Supreme Court, U.S.
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951230 FEB - 1 1996

No. OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1995

BELLSOUTH TELECOMMUNICATIONS, INC., *et al.*,
Petitioners,

v.

FEDERAL COMMUNICATIONS COMMISSION, *et al.*,
Respondents.

Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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PETITION FOR WRIT OF CERTIORARI

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WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

157 pp

QUESTION PRESENTED

The Communications Act provides a private damages action to any person injured by a common carrier's "violation of the provisions of this chapter." 47 U.S.C. § 206. A carrier commits such a violation if it collects an unjust or unreasonable charge for any communications service. 47 U.S.C. § 201(b).

The question presented is whether a carrier may be held *per se* liable for damages solely because its net earnings in a broad category of its services exceeded a rate of return prescribed by the Federal Communications Commission, without further inquiry into whether the carrier's charge for any particular service was unjust or unreasonable or whether the complainant suffered injury as a consequence of the carrier's aggregate net earnings.

PARTIES TO THE PROCEEDING

The following parties appeared as petitioners, respondents, or intervenors in the court below:

Allnet Communication Services, Inc.
Americall Systems of Louisville
American Network Exchange, Inc.
AT&T Corporation
Advanced Telecommunications Corporation and Its Subsidiaries
ATC Long Distance Company
Bell Atlantic Telephone Companies
BellSouth Telecommunications, Inc.
Cable & Wireless Communications, Inc.
Cincinnati Bell Telephone Company
Competitive Telecommunications Association
East Ascension Telephone Company
Federal Communications Commission
First Phone of New England, Inc.
LDDS Communications, Inc.
MCI Telecommunications Corporation
Michigan Bell Telephone Company
MidAmerican Long Distance Company
New England Telephone and Telegraph Company
New York Telephone Company
Nevada Bell
The Ohio Bell Telephone Company
Pacific Bell
Southwestern Bell Telephone Company
Southern New England Telephone Company
Sprint Communications Company, L.P.
Telecom*USA, Inc. and Its Subsidiaries
Telephone Utilities Exchange Carrier Association
U S WEST Communications, Inc.
U S WEST, Inc.
United States of America
United States Telephone Association
Walnut Hill Telephone Company

Set forth below, pursuant to Rule 29.6, is a list of all parent companies and nonwholly owned subsidiaries for each corporate petitioner:

BellSouth Telecommunications, Inc. is a wholly owned subsidiary of BellSouth Corporation, a publicly held corporation.

Cincinnati Bell Telephone Company is a wholly owned subsidiary of Cincinnati Bell Inc., a publicly held corporation.

East Ascension Telephone Company is a privately held corporation. It has no publicly held parent companies, subsidiaries, or affiliates.

Michigan Bell Telephone Company and The Ohio Bell Telephone Company are wholly owned subsidiaries of Ameritech Corporation, a publicly held corporation.

New York Telephone Company and New England Telephone and Telegraph Company are wholly owned subsidiaries of NYNEX Corporation, a publicly held corporation.

Pacific Bell is a wholly owned subsidiary of Pacific Telesis Group, a publicly held corporation.

The Southern New England Telephone Company is a wholly owned subsidiary of Southern New England Telecommunications Corporation, a publicly held corporation.

Southwestern Bell Telephone Company is a wholly owned subsidiary of SBC Communications Inc., a publicly held corporation.

The Telephone Utilities Exchange Carrier Association's member local exchange carriers are: Telephone Utilities of Washington, Inc.; Inter-Island Telephone Company; Peninsula Telecommunications, Inc.; Rose Valley Telephone Company; Telephone Utilities of Eastern Oregon, Inc.; Telephone Utilities

of Oregon, Inc.; Northwestern Telephone Systems, Inc.; Gem State Telephone Utilities Corporation; Eagle Telecommunications, Inc.; Wyoming Telephone Company; and Medicine Bow Telephone Company. These local exchange carriers are wholly owned, through intermediate subsidiaries, by Pacific Telecom, Inc. (PTI). PTI is approximately 87% owned by PacifiCorp Holdings, Inc., a Delaware corporation, which is wholly owned by PacifiCorp, an Oregon corporation, with publicly held and traded debt and equity offerings. The remaining 13% of PTI is held by the public at large and may be traded publicly.

U S WEST Communications, Inc. is a wholly owned subsidiary of U S WEST Communications Group, Inc., which in turn is a wholly owned subsidiary of U S WEST, Inc., a publicly held corporation.

Walnut Hill Telephone Company is a privately held corporation. It has no publicly held parent companies, subsidiaries, or affiliates.

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PETITION FOR WRIT OF CERTIORARI

Twelve local telephone exchange carriers (BellSouth Telecommunications, Inc., Cincinnati Bell Telephone Company, East Ascension Telephone Company, Michigan Bell Telephone Company, New York Telephone Company, New England Telephone and Telegraph Company, Ohio Bell Telephone Company, Pacific Bell, Southern New England Telephone Company, Southwestern Bell Telephone Company, U S WEST Communications, Inc., and Walnut Hill Telephone Company), the Telephone Utilities Exchange Carrier Association,[1] and the United States Telephone Association (USTA)[2] petition for a writ of

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[1] The Telephone Utilities Exchange Carrier Association represents 11 local exchange carriers, each of which is wholly owned by Pacific Telecom, Inc.

[2] USTA is the principal trade association of local telephone companies in the United States. USTA's membership includes nearly

certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App. 1a-26a) is reported at 59 F.3d 1407. While the court of appeals had before it 21 different orders of the Federal Communications Commission, the court specifically considered two FCC orders that set out "the general principles under review." App. 6a. The first of these administrative decisions, *MCI Telecommunications Corp. v. Pacific N.W. Bell Tel. Co.* (App. 27a-74a), is reported at 5 FCC Rcd 216. The second, *MCI Telecommunications Corp. v. Pacific Bell Tel. Co.* (App. 75a-119a), is reported at 8 FCC Rcd 1517.

JURISDICTION

The judgment of the court of appeals was entered on August 1, 1995. Timely petitions for rehearing and rehearing *en banc* were denied on October 4, 1995. App. 120a-123a. On December 20, 1995, the Chief Justice extended the time to file a petition for a writ of certiorari to and including February 1, 1996. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

Section 201 of the Communications Act, 47 U.S.C. § 201, provides, in pertinent part:

> (a) It shall be the duty of every common carrier engaged in interstate or foreign communication by wire or radio to furnish such communication service upon reasonable request therefor . . . .
>
> (b) All charges, practices, classifications, and regulations for and in connection with such communica-

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1100 of the nation's approximately 1350 local telephone companies. The majority of USTA's members are small companies that provide fewer than 10,000 telephone lines.

> tion service, shall be just and reasonable, and any such charge, practice, classification, or regulation that is unjust or unreasonable is declared to be unlawful . . . .

Section 206 of the Communications Act, 47 U.S.C. § 206, provides:

> In case any common carrier shall do, or cause or permit to be done, any act, matter, or thing in this chapter prohibited or declared to be unlawful, or shall omit to do any act, matter, or thing in this chapter required to be done, such common carrier shall be liable to the person or persons injured thereby for the full amount of damages sustained in consequence of any such violation of the provisions of this chapter, together with a reasonable counsel or attorney's fee, to be fixed by the court in every case of recovery, which attorney's fee shall be taxed and collected as part of the costs in the case.

STATEMENT OF THE CASE

The Communications Act is one of several similar federal statutes that provide agencies with carefully circumscribed ratemaking authority.[3] Under the Act, communications common carriers must file tariffs showing all charges for their services and may not collect any charge different from those so specified. 47 U.S.C. § 203(a), (c). Each such charge must be "just and reasonable"; any "unjust or unreasonable" charge "is declared to be unlawful." 47 U.S.C. § 201(b). When a carrier files a new or revised charge, the FCC may investigate the lawfulness of the charge and may temporarily suspend its operation for up to five months pending completion of the investigation. 47 U.S.C. § 204(a)(1). In such a proceeding, the carrier bears the burden of establishing that the charge

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[3] Other such statutes include the Interstate Commerce Act, 49 U.S.C. § 10101, *et seq.*, the Natural Gas Act, 15 U.S.C. § 717, *et seq.*, and the Federal Power Act, 16 U.S.C. § 791, *et seq.*

is just and reasonable. *Id.* If the FCC ultimately finds the charge "not justified," and if the suspension period expired before the proceeding was concluded, the Commission may require the carrier to refund the excessive portion of any charges already collected. *Id.*

If the FCC allows a rate to take effect *without* suspension, it may not thereafter order refunds. *E.g., Illinois Bell Tel. Co. v. FCC*, 966 F.2d 1478 (D.C. Cir. 1992). The Commission may nonetheless investigate such a rate on its own motion or on complaint. If it finds after a hearing that the rate is unlawful, it may direct the carrier to cease collecting the unlawful charge and may prospectively "prescribe what will be the just and reasonable charge . . . to be thereafter observed." 47 U.S.C. § 205(a).

The Act also provides a private damages remedy for any person injured by a carrier's violation of the statute. If a carrier "shall do . . . any act, matter, or thing in this chapter prohibited or declared to be unlawful, or shall omit to do any act, matter, or thing in this chapter required to be done," the carrier "shall be liable to the person or persons injured thereby for the full amount of damages sustained in consequence of any such violation." 47 U.S.C. § 206. A person "claiming to be damaged" may file a complaint either with the Commission or in a federal district court. 47 U.S.C. §§ 207, 208. If the complaint is filed with the Commission, and if the Commission determines that the complaining party has established both a violation of the Communications Act and injury therefrom, then the Commission shall order the carrier to pay the amounts to which the complainant is entitled. *See* 47 U.S.C. § 209.

This case involves a fundamental and recurring question that directly affects communications common carriers and that also implicates other federally rate-regulated industries: May a carrier whose rates have become effective without suspension be held liable for retrospective

damages, not because any particular charge has been found unjust or unreasonable in violation of the statute, but *solely* because the carrier's net earnings for a category of services produced a *rate of return* above some benchmark level set by regulators? Understanding the importance of this question requires a brief discussion of the regulatory framework at issue.

1. The FCC's Rate-of-Return Prescriptions and Refund Remedy

Under traditional ratemaking, a regulated company is entitled to recover its reasonable costs of service, including the opportunity to earn a fair return on invested capital. *See generally FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944). In reviewing the reasonableness of proposed rates, regulators accordingly take into account, among other things, the rate of return that the regulated company needs to attract sufficient capital to provide effective service.

During the 1970s, as part of its oversight of AT&T, the FCC departed from this approach by prescribing in advance a maximum rate of return, thereby "limit[ing] for some period the carrier's discretion to initiate rate revisions" targeted to yield a return above the prescribed level. *Nader v. FCC*, 520 F.2d 182, 201 (D.C. Cir. 1975). Several years later, when AT&T's actual earnings exceeded the prescribed rate of return plus a small margin for error (or "buffer"), the Commission ordered the company to reduce its rates prospectively, in order to offset the prior excess earnings. The D.C. Circuit upheld this approach in *New England Tel. & Tel. Co. v. FCC*, 826 F.2d 1101 (D.C. Cir. 1987), *cert. denied*, 490 U.S. 1039 (1989).

The Commission thereafter sought unsuccessfully to project its theory even further: It adopted an automatic-refund rule, the effect of which was to "extend the use of

the rate of return beyond its role in prospectively determining a carrier's rates." *AT&T v. FCC*, 836 F.2d 1386, 1388 (D.C. Cir. 1988). The Commission required each carrier to compare its actual earnings during a two-year monitoring period with the earnings it would have realized had it achieved its target rate of return plus the specified buffer amount. If a carrier's actual earnings were greater than the target plus the buffer, it was required automatically to surrender the difference in the form of refunds to customers.

The rule required a local exchange carrier to compute refunds separately for each of three different categories of "access services" as well as for its overall interstate operations.[4] Earnings above the authorized rate of return in any segment triggered the refund obligation. Yet earnings *below* the authorized level in a different rate segment, in the carrier's overall operations, or in adjacent monitoring periods could not be used as an offset to negate or reduce a carrier's refund obligation.

The D.C. Circuit struck down the Commission's automatic-refund rule as arbitrary and capricious. The court focused on the asymmetrical operation of the refund mechanism, which "requires the carrier to refund any earnings above the upper bound of target plus buffer, while the carrier may not recoup any shortfall in its earnings below the target." *AT&T v. FCC*, 836 F.2d at 1390. The court found that this imbalance systematically depressed earnings below the federally mandated rate of return over time. *Id.* Since the FCC's rate-of-return pre-

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[4] Long-distance carriers such as AT&T, MCI, and Sprint use a local exchange carrier's access services to carry calls between their long-distance networks and local telephone customers at each end of a long-distance call. The Commission's three access categories are defined by the type of connection provided and the method of computing the applicable charges. Each category typically subsumes numerous rates and service offerings. A single service offering, moreover, may comprise elements from different access categories.

scription embodied its best judgment of "the minimum return the carrier requires," the refund rule "would operate over the long run to put a carrier out of business." *Id.*

Judge Starr concurred in the judgment, but on the broader ground that the FCC lacked statutory authority to attach an automatic-refund rule to rates that have already become effective:

> Congress constructed the Act so that the Commission's remedial power is limited to prospective relief: when the Commission determines that existing rates are excessive, it cannot order a refund of past payments under the revoked rate. Rather, the FCC can only correct the problem through a *prospective* prescription under section 205. The courts have consistently adhered to this basic rule of ratemaking.

836 F.2d at 1394 (citing *Arizona Grocery Co. v. Atchison, T. & S.F. Ry.*, 284 U.S. 370, 390 (1932); *Sea Robin Pipeline Co. v. FERC*, 795 F.2d 182, 189 n.7 (D.C. Cir. 1986)). In a vigorous dissent from the Court's refusal to rehear the statutory issue *en banc*, Judge Starr, joined by Judges Williams and Buckley, further stated that the FCC's refund policy did "violence to well-settled, salutary doctrines, such as the bar on retroactive ratemaking and the filed rate doctrine," and urged that the full court address this "pivotal statutory issue cutting across agency lines." *AT&T v. FCC*, No. 85-1787 (D.C. Cir. filed Nov. 2, 1988) (unpublished).[5]

2. The FCC's Award of Damages for Overearnings

Immediately after the court of appeals invalidated the FCC's automatic-refund rule, MCI and other long-distance companies began filing administrative complaints against local exchange carriers seeking "damages" for earnings

[5] Four members of the court (then-Judge Ruth B. Ginsburg and Judges Silberman, Douglas Ginsburg, and Sentelle) were recused.

above the maximum rate of return. Their theory of liability was materially indistinguishable from the FCC's rationale for automatic refunds. Indeed, they requested as damages the precise amounts they would have received under the automatic-refund rule.

The complaints typically asserted that the defendant carrier had earned in excess of its prescribed rate of return in a particular segment of access service during a particular two-year "monitoring period," that the carrier's charges were therefore unjust and unreasonable in violation of 47 U.S.C. § 201(b), and that the complainant was entitled to damages equal to its proportionate share of the difference between the carrier's actual earnings and its authorized earnings for the segment at issue. The complaints relied exclusively on the carrier's earnings reports filed with the FCC. They alleged no other facts concerning either the reasonableness of the carrier's charges or the extent of any actual injury to the complainant. *See* App. 38a-39a. There was no allegation that any carrier intentionally sought to earn more than the prescribed rate of return or was negligent in setting its rates.

In a series of rulings concerning various years between 1985 and 1990, the Commission held that a carrier whose earnings exceeded the prescribed rate of return in any service category committed a *per se* violation of the statutory requirement that *charges* be just and reasonable, thereby giving rise to an action for damages under Sections 206 and 208. *Id.* at 49a, 84a n.29. The Commission acknowledged that "high profits do not necessarily mean a rate is unreasonable," and it recognized that a *rate-of-return* prescription is not the same as a *rate* prescription. *Id.* at 55a, 63a. It nevertheless concluded that "profits in excess of a prescription are unlawful" and automatically "mak[e] [a carrier's] rates unjust and unreasonable." *Id.* at 55a, 74a.

The Commission further ruled that a complainant need not "establish what a just and reasonable rate would have been as a prerequisite to pursuing damages," because "[t]he issue in these proceedings is not whether individual rates are unlawful, but whether cumulative rates that produced earnings over and above a prescribed rate of return are unjust and unreasonable." *Id.* at 101a-102a. The measure of damages, moreover, was not the difference between the charge collected and a just and reasonable charge, but "the difference between the amount [the complainant] paid for [the carrier's] interstate access services and the amount it would have paid if [the carrier] had charged rates that produced returns within the Commission's prescribed levels"—that is, the amount the customer actually paid less its proportionate share of the carrier's excess earnings for the particular category of charges. *Id.*[6]

The Commission noted, however, that a carrier who earned more than the authorized return in one access category might have earned less than the authorized return in other categories. To take account of a complainant's resulting savings, the Commission allowed carriers to reduce their damage payments "to the extent that it can be shown that [the complainant] benefitted from [the carrier's] undercharges during the relevant period." *Id.* at 111a.

3. The Decision Below

The court of appeals upheld the FCC's findings of liability. Addressing the key statutory issue, the court rejected petitioners' contention that "overearning does not by itself constitute a violation of the Communications Act

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[6] The Commission assumed that, had the carrier's earnings not exceeded the prescribed rate of return, access customers as a whole would have paid an amount equivalent to the amount they actually paid less the amount of the carrier's excess earnings for the particular service category. *See* App. 90a, 112a-114a.

and therefore cannot serve as the sole basis for their damage liability pursuant to § 206." App. 12a. Although nothing in the text of the statute prohibits "overearning," the court held that "a rate-of-return prescription has the force of law" and that "the Commission may therefore treat a violation of the prescription as a *per se* violation of the requirement of the Communications Act that a common carrier maintain 'just and reasonable' rates." *Id.* at 13a.

The court of appeals also concluded that it was not necessary for the Commission to determine a just and reasonable rate before awarding damages. Acknowledging that "both Supreme Court and circuit precedent" require that damages be fixed at "the difference between the charges paid and the just and reasonable rate" (*id.* at 14a (internal quotation marks omitted)), the court nevertheless held that this rule does not apply when an agency regulates by prescribing a rate of return. It may be impossible, the court said, "to know precisely the effect that any given rate will have upon revenues (and therefore upon the [carrier's] rate of return)." *Id.* at 16a. Thus, determining the maximum "just and reasonable" rate may be impossible as well. *Id.* Given this difficulty, the court held, "it seems obvious that the [complainant] could not (or should not be expected to) establish such a rate" as part of its case. *Id.* The court therefore approved the supposedly "conservative" damages formula used by the Commission, under which the percentage by which a carrier overearned for a particular category of access charges is presumptively equal to the percentage by which the complainant was overcharged. *Id.* at 14a-17a.

The court struck down the second part of the Commission's damages formula, under which a complainant's damages for overearnings in one access category were reduced to reflect the carrier's underearnings in other categories. The court viewed such offsets as "an implicit

determination" that the carrier was entitled to earn more than it actually charged for some services. *Id.* at 24a. This result, the court believed, was contrary to a 1965 FCC decision involving carrier "undercharges," incompatible with the Commission's "rate-of-return regime," and—insofar as offsets could be viewed as requiring complainants to pay more for "underpriced" services—inconsistent with the "statutory and regulatory goal of preventing discrimination in the pricing of access services." *Id.* at 23a, 24a, 25a. Under the court of appeals' decision, therefore, carriers may be forced to relinquish in the form of damages any earnings that exceed a prescribed rate of return for a category of access services, but they have no means of recovering, or receiving credit for, earnings below the prescribed rate of return for other access services or for all their services combined.

REASONS FOR GRANTING THE PETITION

The decision below deviates sharply from the terms of the Communications Act and conflicts with the decisions of this Court and lower courts. Under the statute as written, a carrier whose rates have become effective without suspension is entitled to provide service at those rates without risk of retrospective liability, unless the Commission properly determines on complaint both that a specific rate actually charged is unjust or unreasonable and that the unlawful rate has caused actual injury to the complainant. The decision below, however, exposes carriers to *per se* damages liability solely on the basis that their *earnings* for a broad category of services, embracing numerous rates charged to many customers, exceeded a rate of return prescribed by the Commission. Because a carrier's excessive rate of return is not sufficient by itself to establish that any particular rate is unlawful or that any particular complainant has suffered injury, this *per se* rule subjects carriers to liability not intended by Congress.

This question of federal law has great importance for the telecommunications industry. The decision below exposes local telephone companies to massive and unfore-

seeable retroactive liability. The damages awards approved by the court of appeals, though they cover only a portion of the past periods affected by the decision, run against 49 different local telephone companies and total over $83 million plus interest. More than a thousand local exchange carriers face the ongoing threat of recurring, unpredictable liability.[7]

Because of the D.C. Circuit's preeminence in overseeing FCC ratemaking, consideration by other courts of appeals is not likely to resolve this issue. Nor would the telecommunications legislation currently under consideration in Congress affect the statutory provisions or regulatory policies at issue in this petition.

I. THE DECISION BELOW CONFLICTS WITH THE COMMUNICATIONS ACT AND WITH THIS COURT'S DECISIONS ESTABLISHING THAT EXCESSIVE EARNINGS DO NOT MAKE RATES *PER SE* UNLAWFUL

The Communications Act makes carriers liable in damages only for a "violation of the provisions of this chapter"—that is, of the Communications Act itself. 47 U.S.C. § 206. The statute does *not* impose damages liability for violation of an FCC order. It follows that the damages awards at issue here cannot be justified unless petitioners violated some provision of the Communications Act when they realized earnings above their prescribed rate of return.

No provision of the statute limits a carrier's earnings or sets a permissible rate of return. The only mandate that petitioners' earnings can be said to have "violated"

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[7] Since 1991, the largest local exchange carriers have been subject to "price cap" regulation, whereby the FCC prescribes maximum rates rather than maximum rates of return. *See National Rural Telecom Ass'n v. FCC*, 988 F.2d 174 (D.C. Cir. 1993). The FCC's rate-of-return rules continue to apply to all smaller telephone companies, except for a very few that have opted for price cap regulation.

is the FCC's order prescribing their rates of return. But since violation of an FCC order is not a basis for damages under Section 206, the damages awards have no lawful statutory foundation.

The court of appeals nonetheless held that the FCC could properly award damages for violation of a rate-of-return prescription order. The court offered two theories in support of that holding. Neither can be squared with the statute, and each conflicts with decisions of this Court.

A. First, the court stated that "a rate-of-return prescription has 'the force of a statute' and is 'no less binding' than an order establishing the maximum rate that a carrier may lawfully charge." App. 12a (quoting *New England Tel. & Tel. Co. v. FCC*, 826 F.2d at 1107). But to say that an FCC order has "the force of a statute" does not convert the order into a "provision" of the statute. The court's holding collides both with the plain terms of Section 206 and with the Act's overall remedial scheme.

Section 206 allows damages only when a carrier "shall do, or cause or permit to be done, any act, matter, or thing *in this chapter* prohibited or declared to be unlawful, or shall omit to do any act, matter, or thing *in this chapter* required to be done" (emphasis added). The court's theory would effectively recast the italicized phrase, changing it to "in this chapter *or by FCC order*." Moreover, Congress differentiated throughout the Act between violations of the statute and violations of FCC orders, attaching distinct consequences to each.[8] The

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[8] For example, Section 501 provides, in terms identical to Section 206, that any person who "willfully and knowingly" commits an act "in this chapter prohibited or declared to be unlawful," shall be subject to a fine of up to $10,000 and imprisonment for up to two years. By contrast, Section 502 provides that any person who "willfully and knowingly violates any [FCC] rule, regulation,

court's interpretation would obliterate these carefully calibrated remedial distinctions.

By upholding damages for violation of an FCC order, the court of appeals impermissibly indulged the FCC in a "fundamental revision of the statute" based on notions of "desirable policy," the very action condemned by this Court in *MCI Telecommunications Corp. v. AT&T*, 114 S. Ct. 2223, 2232, 2233 (1994).

B. Second, the court of appeals believed that a carrier whose earnings exceeded the prescribed rate of return *must* have charged unreasonably high rates. The court accordingly held that the Commission was free to "treat a violation of the prescription as a *per se* violation of the requirement of [Section 201(b)] that a common carrier maintain 'just and reasonable' rates." App. 13a. Without considering the rates that any carrier had actually charged any particular complainant, the court simply assumed a perfect correlation between excessive earnings and unlawful rates. It thus allowed the Commission to award damages for supposed violations of Section 201(b) based solely on the fact that carriers' earnings in a broad category of services (encompassing numerous customers and many separate charges) exceeded the permissible rates of return established by FCC orders.

This approach suffers from the same analytical defect as the court's "force of statute" theory—it allows com-

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restriction, or condition" shall be subject to a fine of up to $500 per day. Similarly, Section 401(a) authorizes district court mandamus proceedings for "a failure to comply with or a violation of any of the provisions of this chapter," while Section 401(b) separately authorizes district court enforcement proceedings if any person "fails or neglects to obey any order of the Commission." Indeed, Section 205(b) deals specifically with the violation of any rate-of-return prescription promulgated under Section 205(a): it imposes a civil forfeiture of $12,000 per day on any carrier who "knowingly fails or neglects to obey any order made under the provisions of" Section 205. There was no suggestion here, of course, that any carrier "knowingly" disobeyed an FCC prescription order, nor did the FCC purport to impose a civil forfeiture.

plainants to recover damages under Section 206 without making the required showing of unlawful charges and actual injury, and it thereby exposes carriers to liability that was not intended by Congress. Not only is the court's holding at war with the terms of the Communications Act, but it conflicts as well with decisions of this Court and the courts of appeals holding that a carrier's rate of return cannot alone dictate the lawfulness of its charges.

1. This Court has made clear, contrary to the court of appeals' assumption, that a carrier's excessive rate of return does *not* necessarily establish that its rates were unreasonably high. In *Dayton-Goose Creek Ry. v. United States*, 263 U.S. 456 (1924), a railroad challenged a ratemaking scheme under which the Interstate Commerce Commission prescribed uniform rates that allowed railroads, as a group, to receive a fair rate of return. If a particular railroad's earnings exceeded the prescribed rate of return, half of the excess was assigned to a reserve fund maintained for the railroad's own use, and half to a revolving fund administered by the ICC to assist railroads earning less than a fair return.

The Court first upheld the uniform rates prescribed by the ICC as "reasonable from the standpoint of the individual shipper," on the ground that rates permitting a fair return to railroads promote shippers' interest in adequate rail transportation. 263 U.S. at 480. At the same time, however, the Court held that the ICC could lawfully deny the railroads earnings in excess of a "fair or reasonable profit," even though those earnings resulted from charging the prescribed rates. *Id.* at 481. Nor was it necessary to return the excess profits to shippers. Customers, the Court reiterated, did not necessarily suffer injury merely because the carrier earned more than the regulatory maximum:

> The rates are reasonable from the standpoint of the shipper as we have shown, though their net product

> furnishes more than a fair return for the carrier. The excess caused by the discrepancy between the standard of reasonableness for the shipper, and that for the carrier . . . may properly be appropriated by the government for public uses because the appropriation takes away nothing which equitably belongs either to the shipper or to the carrier.

Id. at 484.

Likewise, in *FPC v. Natural Gas Pipeline Co.*, 315 U.S. 575 (1942), the Court made clear that a finding of excessive profits does not entail any specific determination regarding just and reasonable rate levels. The Court there upheld the Federal Power Commission's authority to require a natural gas supplier to reduce its rates prospectively, as the company saw fit, in order to eliminate excessive returns. *Id.* at 583-85. The Court stressed that fixing a rate of return and establishing rates are "two steps of different character." *Id.* at 584. "The first is the adjustment of the general revenue level to the demands of a fair return. The second is the adjustment of a rate schedule conforming to that level so as to eliminate discriminations and unfairness from its details." *Id.* In determining that earning were excessive, the FPC left this second step to the gas supplier. *See id.* at 583. The supplier was not necessarily required to lower every rate, for in identifying excess earnings the FPC did not determine that each rate charged by the supplier was unlawful under all circumstances.

2. Until the decision below, the D.C. Circuit itself had adhered to the principle that a carrier's rate of return does not by itself determine the lawfulness of its filed rates. In *Nader v. FCC*, 520 F.2d at 201, which approved the FCC's prescription of a rate of return for AT&T, the court expressly rejected the "claim that a rate of return is equivalent to rates," holding instead that "a rate of return is merely one component of a rate." 520 F.2d at 201; *see id.* at 203 (rejecting "contention that a

rate of return determination was the same as a determination of rates").

In *Virgin Islands Tel. Corp. v. FCC*, 989 F.2d 1231 (D.C. Cir. 1993), the court likewise stressed that "the prescribed rate of return is but 'one component' of a carrier's tariff schedules." 989 F.2d at 1239 (quoting *Nader*, 520 F.2d at 201). "Projected operating expenses, market forecasts and competitive conditions must also be considered by carriers when they settle on a final access rate." *Id.* The court therefore concluded that, when the FCC determines whether a rate is unjust or unreasonable and (if so) whether a refund is warranted, the Commission must consider not only the prescribed rate of return, but also "other relevant factors." *Id.* Among the factors that "will nearly always be relevant" is "whether the carrier's projections were reasonable at the time they were made." *Id.* at 1240.

In the decision below, the court of appeals attempted to distinguish *Virgin Islands* as involving the Commission's discretionary refund authority under Section 204, rather than an award of damages under Section 206. App. 13a-14a. But the *Virgin Islands* court gathered a number of its "relevant factors"—including the reasonableness of the carrier's revenue projections—from administrative rulings that considered whether a filed rate was just and reasonable (an inquiry that is the same under Section 206 as under Section 204), not whether to award a refund under Section 204. *See Public Serv. Comm'n v. Chesapeake and Potomac Tel. Co.*, 5 FCC Rcd 5518, 5519 (1990); *Western Union Tel. Co.*, 95 F.C.C.2d 881, 910-11 (1983).

3. The Commission's failure to determine what the maximum just and reasonable access rates would have been also conflicts with this Court's interpretations of the Interstate Commerce Act (ICA). Under the ICA, regulators must determine what rate would have been reasonable before they may award damages for excessive rates,

because shippers are afforded a cause of action for damages "in the amount of the difference between the tariff rate and the rate determined to be reasonable by the ICC." *Reiter v. Cooper*, 113 S. Ct. 1213, 1217 (1993); *see Meeker v. Lehigh Valley R.R.*, 236 U.S. 412, 428 (1915) (ICC must determine reasonable rate in order to award damages for excessive rate); *accord United States v. Associated Transport, Inc.*, 505 F.2d 366, 369 (D.C. Cir. 1974) (same). The damages provisions of the Communications Act were derived from the ICA, and cases interpreting the analogous provisions of the ICA provide "guidance in interpreting the Communications Act." App. 22a; *see MCI Telecommunications Corp. v. AT&T*, 114 S. Ct. at 2231 (ICA served as "model" for Communications Act).

In the decision below, the court of appeals acknowledged that "the ratemaking agency must establish the just and reasonable rate in order to calculate damages" (App. 15a), but it held that the rule could be waived in a case involving overearnings. According to the court, it would be unfair to enforce this statutory mandate because "requir[ing] the [complainant] to establish the rate that would have produced only a reasonable rate of return for the [carrier] would be to ask of it the very thing that the [carrier] was itself unable to do." *Id.* Noting that any reasonable rate fixed by the FCC would necessarily be "an estimate," the court inferred that the Commission should likewise be free to use an estimate to assess damages, and that the agency could therefore accept the complainants' "conservative" calculation without violating statutory requirements. *Id.* at 17a.

As this Court's decisions under the ICA hold, the statute does not permit such shortcuts. Whatever room the agency may have to employ estimates in determining a reasonable rate, it may not leapfrog that requirement and assess damages on some other basis. That is particularly so in this case because the logic that the damages

awarded against petitioners were "conservative" is incorrect on its own terms.

The court of appeals stressed that demand varies inversely with price, so that a reduction in a carrier's access rates would likely stimulate greater demand for its services. *Id.* at 16a-17a. From that premise, the court concluded that an inquiry into the actual reasonable rate for specific services would show greater damages than the FCC awarded. Because sales increase as price falls, it reasoned, carriers would have had to lower their rates by more than the percentage of their overearnings to bring their rate of return down to authorized levels. *Id.* at 17a.

The court mistakenly assumed that the only possible result of reducing rates is a more gradual *decrease* in carrier earnings. *Id.* But reducing rates may *increase* earnings instead. If the percentage increase in demand is greater than the percentage decrease in price, a seller can increase its revenues—and perhaps its profits—by lowering its price. *See* Samuelson & Nordhaus, *Economics* 69 (14th ed. 1992); Baumol & Blinder, *Economics Principles and Policy* 468-72 (5th ed. 1991). It is simply impossible to determine without case-by-case analysis whether, in any particular market setting, a rate reduction would have produced a net increase or a net decrease in earnings. *See* 2 Kahn, *The Economics of Regulation* 102-103 (MIT Press 1988).

If reducing rates for a particular access service would have increased the carrier's earnings, then (under the court's logic) customers of that service may have been *under*charged rather than *over*charged. Yet the court of appeals held that injury can be established simply from the fact of excess earnings in a category of access services, without any case-by-case consideration. This "close enough" approach is irreconcilable with the Commission's duties under Section 206.

II. THE DECISION BELOW CONTRAVENES THE STATUTORY SCHEME BY RENDERING CARRIERS RETROSPECTIVELY LIABLE FOR EVENTS THAT ARE BEYOND THEIR CONTROL

Certiorari also should be granted because the decision below upsets "the values of stability and predictability that Congress so carefully enshrined in the Communications Act." *AT&T*, 836 F.2d at 1394 (Starr, J., concurring). The statutory scheme allows carriers to calculate the just and reasonable rate in the first instance, subject to administrative suspension and investigation under Section 204. The burden of proof in such a proceeding is on the carrier. 47 U.S.C. § 204(a). But if the rate becomes legally effective, the burden shifts to the complaining party, who must prove both that the rate is unjust or unreasonable and that it has caused compensable injury. *Aeronautical Radio, Inc. v. FCC*, 642 F.2d 1221, 1235 n.34 (D.C. Cir. 1980), *cert. denied*, 451 U.S. 920 (1981); *see also Arizona Grocery Co. v. Atchison, T. & S.F. Ry.*, 284 U.S. 370, 384 (1932) (shipper bound to pay the lawful rate, "but if he could show that it was unreasonable, he might recover reparations"). These provisions subject carriers to liability only for a failure to do what is directly within their power (file a just and reasonable rate).

The decision below, by contrast, exposes common carriers to *per se* liability for events they cannot control. Because carriers cannot predict with any certainty their costs and the demand for their services, they cannot reliably determine their rate of return until after the relevant monitoring period is over. Carriers thus may be powerless to head off liability for violations of the FCC's rate-of-return prescription.

The Sixth Circuit has explained some of the problems with imposing retrospective liability for overearnings. In *Ohio Bell Tel. Co. v. FCC*, 949 F.2d 864 (6th Cir. 1991), that court expressly followed the D.C. Circuit's *AT&T* decision and held that communications common

carriers may not be required to refund earnings above the prescribed rate of return unless they are allowed to recover shortfalls below the prescribed rate of return. *Id.* at 872-74.[9] The court explained that carriers "calculate [their] rates so that the projected revenues will cover projected operating expenses, including the authorized return on capital." 949 F.2d at 867. But it is exceedingly rare that the carrier's estimates of costs and demand prove exactly correct. *Id.* "[B]ecause of the indeterminacy of the figures used in the calculations, carriers will virtually never earn precisely their authorized rate of return." *Virgin Islands*, 989 F.2d at 1233.[10]

In partial recognition of this uncertainty, the FCC allows carriers a small buffer above the prescribed rate of return and affords some limited opportunities for adjusting rates to compensate for prior overearnings or underearnings within the same monitoring period. *See id.* But these measures do not cure the problem of unpredictable returns. Carriers "have consistently deviated from the authorized return by far more than the buffer amount." *AT&T*, 836 F.2d at 1390 n.4. Indeed, in *New England Telephone*, Judge Buckley described earnings above the prescribed rate of return as "a central feature of rate-of-return regulation." 826 F.2d at 1114 (Buckley, J., dissenting).

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[9] In the decision below, the D.C. Circuit attempted to distinguish *Ohio Bell* (and its own holding in *AT&T*) as resting on an obsolete interpretation of FCC rules. App. 10a. In fact, however, *Ohio Bell* was argued and decided *after* the 1990 FCC decision that, according to the D.C. Circuit, established a new Commission policy. *Compare* App. 8a-9a (quoting FCC decision) *with* 949 F.2d at 873 (noting Commission's failure to offer "argument or authority" in defense of refund policy).

[10] The *Virgin Islands* case provides a particularly glaring illustration. After Hurricane Hugo destroyed well over half the telephone lines on St. Croix and St. Thomas, the carrier raised its access rates in the expectation that demand for long distance calls would fall. In fact, demand was unexpectedly above normal after the hurricane, while the telephone company (which had half of its equipment out of service) had below-normal operating costs. As a result, the carrier's earnings far exceeded its FCC-prescribed rate of return. *See* 989 F.2d at 1234-36.

Traditionally, when a carrier recovered excessive earnings from rates that had not been set aside as unreasonable, the Commission adjusted the carriers' rates prospectively to prevent future overearnings. The carrier was not subject to retrospective liability for such overearnings, just as its customers were not subject to retrospective liability for the carrier's underearnings. *See Ohio Bell,* 949 F.2d at 867. Even when the D.C. Circuit upheld future rate reductions to make up for past overearnings in *New England Telephone*, it predicated its decision on 47 U.S.C. § 154(i)—the Communications Act's "necessary and proper" clause—leaving the Commission discretion to fix a customer's recovery at a level that accounts for equitable considerations such as the carrier's good-faith attempts to comply with the rate-of-return prescription.

Section 206 denies the Commission any such flexibility. The court of appeals, moreover, invalidated the Commission's offsets, by which the FCC reduced the complainants' damages awards by millions of dollars to reflect underearnings (and, therefore, presumptive underpayments) for other categories of access services. Under the holding of the court of appeals, a complainant may recover for presumed overcharges in a category of services even though the carrier's predictions of costs and demand were beyond reproach, and even though the complainant lawfully could have been charged more than it paid when all three access categories are taken into account. Carriers must therefore pay out their overearnings in each category in the form of damages without any opportunity to recover their underearnings in other categories or in their overall operations. The outcome is the same as the one found unacceptable in *AT&T* and *Ohio Bell*: Profits will be systematically depressed below the authorized rate of return.

The decision below denies carriers the rate stability built into the Communications Act. Carriers that calculate their rates to achieve the prescribed rate of return, properly file those rates with the Commission, see them become effective without suspension under Section 204,

and then lawfully charge the filed rates will nonetheless routinely be held retroactively liable because they operated more efficiently than expected or sold more of their services than anticipated. In order to avoid such liability, carriers will have to aim systematically below the authorized rate of return, causing them to earn less, on a long-term basis, than the rate of return deemed appropriate by federal regulators.

As defendants in such suits, moreover, carriers will lack the procedural protections Congress built into Section 206. The Commission's *per se* approach lifts from complainants the burden of proving, based on all the relevant facts, that a legally effective rate is unlawful and that they were injured thereby. It frees the Commission from determining what a just and reasonable rate would be. And the *per se* rule (as enforced by the court of appeals) prevents the Commission even from taking into account underearnings on other categories of access services purchased by a particular customer, leaving the complainant with an undeserved windfall.

Certiorari is warranted to clear this cloud of unforeseeable and largely unpreventable retrospective liability and to restore the clear statutory rules that Congress established for rate-regulated carriers.

CONCLUSION

The petition for writ of certiorari should be granted.

Respectfully submitted,

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APPENDICES

APPENDIX A

UNITED STATES COURT OF APPEALS
DISTRICT OF COLUMBIA CIRCUIT

Nos. 93-1166, 93-1191, 93-1223, 93-1224, 93-1234, 93-1235, 93-1236, 93-1237, 93-1238, 93-1239, 93-1280, 93-1281, 93-1282, 93-1287, 93-1288, 93-1353, 93-1418, 93-1427, 93-1446, 93-1462, 93-1527, 93-1528, 93-1529, 93-1530, 93-1531, 93-1532, 93-1535, 93-1536, 93-1537, 93-1538, 93-1539, 93-1540, 93-1541, 93-1542, 93-1543, 93-1544, 93-1545, 93-1546, 93-1559, 93-1598, 93-1606, 93-1607, 93-1608, 93-1609, 93-1613, 93-1644, 93-1677, 93-1685, 93-1825, 94-1123, 94-1124 and 94-1332

MCI TELECOMMUNICATIONS CORPORATION, *et al.*,
Petitioners,

v.

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA,
Respondents,

PACIFIC BELL, *et al.*,
Intervenors.

On Petitions for Review of Orders of the
Federal Communications Commission

Argued April 11, 1995

Decided August 1, 1995

Before: EDWARDS, Chief Judge; WALD and GINSBURG, Circuit Judges.

Opinion for the Court filed by Circuit Judge GINSBURG.

GINSBURG, Circuit Judge:

In these consolidated cases, we review 21 orders of the Federal Communications Commission adjudicating damage actions filed by several interexchange carriers (IXCs) alleging that various local exchange carriers (LECs) overcharged them for interstate access services. The LECs ask us to set aside the 21 orders on the ground that the Commission's approach to awarding damages is unlawful and most of the IXCs' damages claims are barred by the statute of limitations. The IXCs want us to modify the Commission's orders only insofar as they allow the LECs to take "limited offsets" against the damage awards to the IXCs. One IXC (Allnet Communication Services, Inc.) argues in the alternative that if limited offsets are to be allowed, then the Commission should increase the interest rate payable on its award of damages. Because we conclude that the Commission's general approach to damages is not unlawful and that the IXCs' claims are not barred by the applicable statute of limitations, we deny the petitions of the LECs in their entirety. Because we agree with the IXCs that the Commission's limited offset policy is unlawful, we grant the IXCs' petitions with regard to that issue, vacate the Commission orders in part, and remand these matters to the Commission to recalculate the IXCs' damages. Allnet's petition is dismissed as moot in view of our decision invalidating limited offsets.

I. BACKGROUND

Interexchange carriers such as petitioner MCI pay LECs for access to local telephone users. From the mid-1970's until the early 1990's the Commission's primary method for regulating the price of interstate access was

to prescribe a maximum rate of return on equity that a LEC could earn from the sale of interstate access over a given period of time. *See National Rural Telecom Ass'n v. F.C.C.*, 988 F.2d 174 (D.C.Cir.1993) (reviewing the Commission's later switch from rate-of-return to price-cap regulation). The claims at issue here are based upon certain LECs' having earned rates of return above the maxima prescribed by the Commission. In order properly to understand those claims, however, the reader may find an abbreviated regulatory history helpful.

A. *Regulatory History*

In 1972 the Commission decided that rather than prescribe the rates that AT & T could charge it would prescribe the maximum rate of return that AT & T could earn (8.5%) and leave it to the carrier to set its rates at a level designed to yield up to the prescribed rate of return. *See American Tel. & Tel. Co. and the Assoc. Bell System Companies, Charges for Interstate Telephone Service, Decision and Order,* Docket No. 19129, 38 F.C.C.2d 213 (1972). Upon review, we upheld this rate-of-return approach as an appropriate exercise of the Commission's general regulatory powers under § 4(i) of the Communications Act, 47 U.S.C. § 154(i). *See Nader v. F.C.C.*, 520 F.2d 182, 203-04 (1975).

In 1976 the Commission raised AT & T's allowable rate of return to 9.5%, *American Tel. & Tel. Co., Charges for Interstate Telephone Services, Decision,* Docket No. 20376, 57 F.C.C.2d 960, 972-73 (1976), plus a buffer of .5% inasmuch as it announced that it would not take enforcement action unless the Company's return actually exceeded 10%. *Id.* at 973. AT & T thereupon filed a tariff structure that produced a return below 10% for 1976 and 1977, but in 1978 the same rates produced a return above the 10% ceiling. The Commission responded by requiring AT & T (and the post-divestiture Bell Operating Companies) to return their excess earnings to customers by reducing future rates.

AT & T Earnings of Interstate and Foreign Services During 1978 Decision, CC Docket No. 79-187, 102 F.C.C. 2d 52, 62-63 (1984). AT & T challenged the Commission's statutory authority to require such a refund, but the court upheld the FCC's authority to impose that remedy, again pursuant to § 4(i). *New England Tel. & Tel. Co. v. F.C.C.*, 826 F.2d 1101, 1106-09 (D.C.Cir. 1987) (*NETCO*).

By the time the court published its decision in *NETCO*, however, the Commission had already changed course, establishing a more comprehensive approach to regulating the LECs' rate of return. *See Authorized Rates of Return for the Interstate Services of AT & T Communications and Exchange Telephone Carriers, Phase I, Report & Order*, CC Docket No. 84-800, 58 Rad.Reg.2d 1647 (P & F) (1985) (*Prescription Order*), *recon., Memorandum Opinion & Order*, 59 Rad.Reg.2d 1592 (P & F) (1986) (*Prescription Reconsideration*). The Commission still prescribed a maximum rate of return that a LEC could earn from the sale of interstate access overall, but now it also set a maximum rate of return for each of three specific types of interstate access service (*viz.*, "special," "common line," and "switched traffic sensitive") and established a refund mechanism whereby a LEC would automatically be required at the end of a monitoring period to refund all revenues that it had collected above the amount corresponding to its allowed rate of return for each category. *Prescription Reconsideration*, 59 Rad.Reg.2d at 1604. Thus, a LEC could be required automatically to refund its excess earnings for one type of access service even if its earnings from the provision of excess services overall were below the maximum rate of return allowed. The Commission recognized this possibility, but explained that categorical (*i.e.*, type-specific) rate-of-return prescriptions were necessary in order to prevent rate discrimination: without them, the LECs could charge an excessive rate to purchasers of one type of access in order to subsidize the

rate charged to purchasers of another type. *Id.* at 1603. Upon review this court held, following *NETCO*, that the Commission has the statutory authority both to prescribe a rate of return and to order a refund when that prescription is violated; at the same time we held that the Commission's decision to require automatic refunds for each category in which a LEC overearned was arbitrary and capricious and therefore unlawful because that mechanism was inconsistent with what the court perceived to be the Commission's general approach to rate-of-return regulation. *American Tel. & Tel. Co. v. FCC*, 836 F.2d 1386, 1390-92 (1988) (*AT & T*).

B. *The Present Proceedings*

Although the court overturned the automatic refund rule, it did not strike down the rates of return that the Commission had authorized, either for access service in general or for any specific type of access. The Commission therefore continued to set general and categorical rates of return that limited the amount that a LEC could earn over any given two-year monitoring period. For example, for the 1987-88 and 1989-90 monitoring periods, the Commission prescribed a maximum rate of return of 12% both for overall earnings and for each type of service, and added enforcement buffers of .25% for overall earnings and .4% for each category. *See Authorized Rates of Return for the Interstate Services of AT & T Communications and Exchange Telephone Carriers, Phase III, Memorandum Opinion & Order*, CC Docket No. 84-800, 60 Rad.Reg.2d 1589, 1607 (P & F) (1986) (setting percentage rates of return for 1987-88); *American Tel. & Tel. Co. v. Central Tel. Co., et al., Memorandum Opinion & Order*, 8 F.C.C.R. 3546, 3547 (1993) (observing that rates of return for 1987-88 period were extended through 1989-90 period).

Shortly after the court's decision in *AT & T*, the IXCs began to file complaints with the Commission, pursuant to §§ 206-09 of the Communications Act, 47 U.S.C.

§§ 206-09, seeking damages from each LEC that had allegedly overcharged the IXCs for access service because it had earned (either for a category of service or overall) more than the maximum allowable rate of return for the monitoring period. The IXCs based their allegations upon the reports that the LECs are required to file with the Commission after the end of each monitoring period; the IXCs alleged (and most LECs conceded) that they reported earnings in excess of the maximum prescribed levels. The complaints at issue here relate to the monitoring periods 1985-86, 1987-88, and 1989-90.

Although the Commission adjudicated the complaints separately and the details of each differ somewhat, the agency set forth the general principles under review here in two orders, both of which pertain to the claims made by MCI. *See MCI Telecommunications Corp. v. Pacific Northwest Bell Tel. Co., et al., Memorandum Opinion & Order*, 5 F.C.C.R. 216 (1990) (*MCI Liability Order*); *MCI Telecommunications Corp. v. Pacific Bell Tel. Co., et al., Memorandum Opinion & Order*, 8 F.C.C.R. 1517 (1993) (*MCI Damages Order*). In those orders (as in the others under review) the Commission held that a LEC that earns in excess of the prescribed rate of return (either for a category or overall) for a monitoring period violates the Communications Act. *MCI Liability Order*, 5 F.C.C.R. at 223. The Commission further held that "the proper starting point for assessing damages based on violations of a rate of return prescription is to look at the difference between the amount [the IXC complainant] paid for [the defendant LEC's] interstate access services and the amount it would have paid if [the LEC] had charged rates that produced returns within the Commission's prescribed levels." *MCI Damages Order*, 8 F.C.C.R. at 1525. The Commission then allowed each defendant LEC to take "limited offsets," meaning that the defendant LEC could subtract from the amount that the IXC overpaid, as derived above, any amount that the same IXC customer had "underpaid" the LEC (*i.e.*, insofar as

it had paid a rate that yielded a return below the prescribed maximum) for any category of service during the same monitoring period. *Id.* at 1528.

II. ANALYSIS

The LECs and the IXCs both attack the Commission's rules, albeit from opposite directions. The LECs seek vacatur of some if not all of the damage decisions, while the IXCs ask us effectively to increase the amount of damages awarded in most of the cases.

A. *The LECs' Claims*

The LECs contend that: (1) the Commission's approach to damages is precluded by our decision in *AT & T*; (2) the Commission improperly concluded that LEC earnings in excess of the allowed rates of return are *per se* unlawful; (3) the Commission improperly allowed the IXCs to recover damages without requiring them each to show what would have been the just and reasonable rate and by exactly how much it overpaid; and (4) most of the damage claims are barred by the two-year statute of limitations in the Communications Act. None of these assertions has merit.

1. *The teaching of* AT & T

The LECs argue that all of the damage awards should be reversed because they are functionally equivalent to the automatic refund remedy that we disapproved in *AT & T*. The LECs' argument fails because, the question of functional equivalence quite apart, it proceeds from a misunderstanding of our *AT & T* decision.

In *AT & T* we took issue with the automatic refund rule because it required a LEC to refund earnings to the extent that it earned more than the allowable rate of return for a particular type of service without any offset for any types of service in which the LEC had earned less than the allowable rate of return. That approach

"virtually guaranteed" that the LECs would earn an aggregate rate of return below that which the Commission had prescribed. *AT & T*, 836 F.2d at 1390-91. The LECs suggest that we thereby fashioned a broad rule prohibiting the Commission from awarding damages for overearnings in one category of service without allowing a LEC to offset all underearnings that it had for other categories. On the contrary, our holding was much more narrow: The Commission's approach was unlawful because it was inconsistent with what we were told was the Commission's own understanding of its rate-of-return regulation. *Id.* at 1390-91. We believed—based upon certain FCC ratemaking orders and upon representations by the Commission's counsel at oral argument—that the Commission viewed its rate-of-return prescriptions as stating not only the maximum that a LEC could reasonably charge its customers but also the minimum that the LEC could charge and still attract investment capital. *Id.* at 1390. We therefore held that a refund rule that would inevitably cause the LEC to earn an overall rate of return below the prescribed level was unreasonable because it amounted to a "self-contradiction" and "would operate over the long run to put [the LECs] out of business." *Id.* at 1390-91.

The Commission responded to our decision by "clarify-[ing]" its view of rate-of-return regulation, as follows:

> [W]e do not view [the rate-of-return] prescription as "both a maximum and a minimum." That is, it does not represent a unique balance point such that "if the rate were higher, the balance would tip in favor of the investor; if lower, it would tip in favor of the consumer." Our accumulated experience with rate of return prescriptions, and our review of the cost of capital evidence in this proceeding, convince us that there is no such point. Indeed, even the lower boundary of our range of cost of capital estimates does not represent a bright line such that a company

> earning just below that level would be forced out of business. We believe there is a substantial gap between an earnings level that is fully adequate to assure attraction of capital on favorable terms, and an earnings level which, if sustained over time, would be confiscatory.

Represcribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers, Order, CC Docket No. 89-624, 5 F.C.C.R. 7507, 7532 (1990); *accord Amendment of Parts 65 and 69 of the Commission's Rules to Reform the Interstate Rate of Return Represcription and Enforcement Processes, Notice of Proposed Rulemaking and Order*, CC Docket No. 92-133, 7 F.C.C.R. 4688, 4701 (1992).

This clarification is critical for two reasons. First, it allays any concern with "self-contradiction": Even if the Commission's new approach has the same effect as did the automatic refund rule in *AT & T*, that outcome no longer appears to be inconsistent with the Commission's view of how rate-of-return regulation should work. Second, it removes the premise from which the *AT & T* court reasoned that the refund rule would operate over the long run to put LECs out of business. It is, of course, still true that by awarding damages on a category-by-category basis while allowing only limited offsets—*viz.*, offsets for "underpayments" made by the same customer for other access services during the same monitoring period—the Commission's approach to damages has caused many LECs to earn, in the aggregate, less than the maximum rate of return allowed for the monitoring period(s) at issue. As the Commission's approach has been clarified, however, that does not necessarily mean that any LEC earned less than the minimum amount necessary to attract capital and, in fact, no LEC has demonstrated that its rate of return (*i.e.* net of damage awards) was unreasonably low. Indeed, the LECs make no factual showing at all with respect to that issue. Hence, even assuming *arguendo*

that the Commission's approach to awarding damages is functionally equivalent to the automatic refund remedy held unlawful in *AT & T*, that is no warrant for striking down the Commission's damage awards here. As we explained in *NETCO*, the LECs "have no statutory entitlement to a perfectly balanced regulatory regime; rather they are entitled only to earn an overall reasonable return." 826 F.2d at 1108-09.

The LECs offer up the Sixth Circuit's decision in *Ohio Bell Tel. Co. v. F.C.C.*, 949 F.2d 864 (1991), and our decision in *Virgin Islands Tel. Corp. v. F.C.C.*, 989 F.2d 1231 (1993), as further support for their claim that the Commisson must allow a LEC to offset against an award of damages for overearnings on one type of service any underearnings that it had for other types. Although *Ohio Bell* involved an individual refund rather than the general, automatic refund provision, the Sixth Circuit expressly followed our decision in *AT & T;* it held that it is inconsistent with the Commission's own rate-of-return regulatory policy for the Commission to require that a LEC refund overearnings on a category-by-category basis without allowing it to offset underearnings in other categories of interstate access service. *Id.* at 872-74. So far as the opinion reveals, however, the Sixth Circuit was not aware of the Commission's clarifying statement; that court appears to have believed, as had we in *AT & T*, that the Commission regarded the target rate of return as both a maximum and a minimum. That premise having since been removed, *Ohio Bell* does not advance the LECs' argument any further than does *AT & T*.

We are quite frankly mystified by the LECs' attempt to draw support from our *Virgin Islands* decision. In that case we reversed a Commission order that required a LEC to refund interstate access earnings that were running above the prescribed rate of return as of the middle of an on-going monitoring period—a factual situation not present in any of the cases before us now. Indeed, in

reversing the Commission we explained that its decision to require a refund in the middle of the monitoring period was "analogous to that of a parent who admonishes his child not to eat more than one candy bar per day and then concludes that the prescription has been violated when he observes the child eat his first half of a candy bar in one minute." 989 F.2d at 1238. Moreover, we explained that "*AT & T* . . . emphasized that the Commission's authority to order refunds where a carrier has violated an outstanding rate-of-return prescription 'must . . . be exercised in a way that does not contradict the Commission's own theory of rate of return regulation.'" *Id.* at 1234 (quoting *AT & T*, 836 F.2d at 1392). The *Virgin Islands opinion*, therefore, only strengthens our view that *AT & T* was based narrowly upon the apparent conflict between the Commission's automatic refund and its own rate-of-return philosophy, as we then understood it, and not upon the LECs' broader reading of that case.

Petitioner Cincinnati Bell Telephone Company makes a separate argument that differs from that of the other LECs only in emphasis. Because Cincinnati Bell had overearnings for all three types of access service during the 1987-88 monitoring period, it focuses not upon offsets among types of services but upon the Commission's refusal to allow it to offset earnings below the prescribed rate of return for prior and subsequent monitoring periods. Its argument that such offsets are required under *AT & T*, however, relies upon the very interpretation of that case that we rejected above; we therefore find Cincinnati Bell's separate argument unconvincing.

2. *The Commission's approach to establishing a violation of the act*

The IXCs base their damage claims upon § 206 of the Communications Act, which provides:

> In case any common carrier shall do . . . any act, matter, or thing in this [Act] prohibited or declared

> to be unlawful . . . such common carrier shall be liable to the person . . . injured thereby for the full amount of damages sustained in consequence of any such violation of the provisions of this [Act]. . . .

47 U.S.C. § 206. Although the LECs' earnings exceeded the maximum rates of return prescribed by the Commission, they contend that such overearning does not by itself constitute a violation of the Communications Act and therefore cannot serve as the sole basis for their damage liability pursuant to § 206. We disagree.

As discussed above, in *NETCO*, 826 F.2d at 1106-07, we held that the Commission has the statutory authority to prescribe a carrier's maximum rate of return and to require a LEC that fails to comply to refund earnings in excess thereof. More important, we held that:

> The Commission's chief concern in issuing [rate-of-return] prescriptions is protecting just and reasonable rates. . . . The idea of a prescription . . . is that the agency has proclaimed that a certain situation—here a return in excess of 10%—is unlawful and *shall not occur.*

Id. at 1106 (emphasis in original). Relying upon our earlier decision in *Nader* we further explained that a rate-of-return prescription has "the force of a statute" and is "no less binding" than an order establishing the maximum rate that a carrier may lawfully charge. *Id.* at 1107. In *AT & T* we reconfirmed all this, explaining that in *Nader* we had held "that the Commission has power under [the Communications Act] to prescribe rates of return as well as rates," and that in *NETCO* we had held that the "prescription of a rate of return . . . represent[s] a proclamation by the Commission that earnings in excess of the prescribed rate are unlawful. . . ." 836 F.2d at 1392. Hence, all these cases—*Nader, NETCO,* and *AT & T*—stand squarely in opposition to the LECs' position:

We have repeatedly held that a rate-of-return prescription has the force of law and that the Commission may therefore treat a violation of the prescription as a *per se* violation of the requirement of the Communications Act that a common carrier maintain "just and reasonable" rates, *see* 47 U.S.C. § 201(b).

The LECs attempt to avoid this seemingly inevitable conclusion by relying once again upon our *Virgin Islands* decision. There, after holding the Commission's refund order invalid because it was imposed as of the middle of a monitoring period, we went on to note that:

> the prescribed rate of return is but "one component" of a carrier's tariff schedules. Projected operating expenses, market forecasts and competitive conditions must also be considered by carriers when they settle on a final access rate. Given this multitude of inputs, the prospective selection of a tariff that will generate the prescribed rate of return is necessarily an imprecise endeavor. Thus, once the Commission finds that a carrier has exceeded (as a pure mathematical matter) its prescribed rate of return, it should then consider other relevant factors in determining whether a rate is unreasonable and a refund warranted.

989 F.2d at 1239. We also went on to list the sort of factors that the Commission should consider in deciding whether to order a refund, including: (1) whether the LEC's projections were reasonable when made; (2) the actual harm suffered by the ratepayer; and (3) any "overriding equitable considerations." *Id.* at 1240.

Seen in context, however, we do not think that our *Virgin Islands* decision is a bar to the Commission's decision to treat earning more than the prescribed rate of return as a *per se* violation of the Act for the purpose of adjudicating a damage claim. *Virgin Islands* arose under § 204 of the Communications Act, which provides

that, under certain circumstances, the Commission itself "may . . . require [a carrier that has collected an excessive amount] to refund, with interest, . . . such portion of such charge . . . as by its decison shall be found not justified." 47 U.S.C. § 204. Because the § 204 refund remedy is couched in permissive terms, the court was in effect advising the Commission of the issues it must consider in exercising its discretion whether to require a refund. In the present cases, by contrast, the Commission is responding to complaints brought by customers of the LECs under § 206 of the Act, which is phrased in mandatory terms: A carrier that has violated the Act "shall be liable to the person or persons injured thereby for the full amount of damages sustained in consequence of any such violation . . . ." 47 U.S.C. § 206. Therefore, the factors that we set out in the *Virgin Islands* case do not apply where, as here, the Commission is adjudicating a damage claim made by a customer pursuant to § 206.

3. *Equating damages (before limited offsets) with earnings in excess of prescribed rates of return*

Closely related to the LECs' argument against liability for overearning is their claim that, in order to calculate its damages, an IXC must identify the specific rate that the LEC could reasonably have charged it. They contend that this is required by both Supreme Court and circuit precedent, which teaches that a customer's damage is the "difference between the charges paid and the just and reasonable rate[]." *United States v. Associated Transport, Inc.*, 505 F.2d 366, 369 (D.C.Cir.1974); *see also Reiter v. Cooper* —— U.S. ——, ——, 113 S.Ct. 1213, 1217, 122 L.Ed.2d 604 (1993); *Meeker v. Lehigh Valley R.R. Co.*, 236 U.S. 412, 428, 35 S.Ct. 328, 334, 59 L.Ed. 644 (1915); *Oneida Motor Freight, Inc. v. I.C.C.*, 45 F.3d 503, 507 (D.C.Cir.1995).

What the Commission actually did was something rather different. In order to arrive at an initial (*i.e.*, pre-offset)

figure the Commission assumed that an IXC's damages are equal to (1) the aggregate amount that the IXC paid the LEC for a specific category of access service, (2) less the aggregate amount that the IXC would have paid for that service had the LEC charged the IXC a rate that would have produced earnings at the maximum allowed rate of return. *MCI Damages Order*, 8 F.C.C.R. at 1525. That would be a way of calculating the difference between the charges paid and the just and reasonable rate, but the Commission did not require the IXCs actually to make this precise calculation. Rather, for simplicity, the Commission allowed each IXC to approximate that calculation by multiplying the percentage amount by which the LEC overearned—the difference between the LEC's actual and prescribed rates of return—times the total dollar amount that the IXC paid for that type of access. *See, e.g., MCI Damages Order*, 8 F.C.C.R. at 1521-22, 1525.

The cases cited by the LECs do state that the rate-making policy must establish the just and reasonable rate in order to calculate damages, but that is all that they say. They do not discuss this requirement in any detail, and none of them involves a situation in which the regulatory agency had prescribed a binding rate of return rather than an actual rate. Therefore they do not address, let alone answer, the fundamental question at issue here—whether an agency that regulates by prescribing a rate of return may allow a customer that was overcharged because the carrier earned more than its allowed rate of return, rather than deriving an actual rate, to make a simplifying assumption about what the reasonable rate would have been.

In support of its simplified approach, the Commission notes that to require the complaining IXC to establish the rate that would have produced only a reasonable rate of return for the LEC would be to ask of it the very thing that the LEC was itself unable to do. *MCI Damages Order*, 8 F.C.C.R. at 1525. The Commission rejected that idea because, as it said with admirable restraint:

> [I]t would be inequitable to permit defendants [the LECs], who were in the best position to set their rates at lawful levels in the first place, and who later had opportunities to correct those rates, to avoid responsibility for those unlawful rates, at the expense of their customers.

Id. The Commission's point is as well-taken as the LECs' is absurd. During any monitoring period in which its rates appeared destined to yield earnings above (or for that matter below) its authorized rate of return the LEC could have revised its tariffs to avoid that result. *See Prescription Order,* 58 Rad.Reg.2d at 1653-54 (P & F). Moreover, by incorporating a buffer into its rate-of-return prescriptions the Commission had allowed each LEC some margin for error. These provisions afforded each LEC considerable flexibility to use the market information available to it—the LEC presumably knew at least approximately what its revenues and costs were—to fashion a rate that was "reasonable," *i.e.,* would not result in a return above the maximum allowed. If the LEC, with its superior information, could not (or did not) accurately establish such a rate, then it seems obvious that the IXC could not (or should not be expected to) establish such a rate from the outside looking in.

Admittedly, any calculation of the rate that will produce a targeted rate of return, whether it is done by the Commission, an IXC, or for that matter a LEC, is necessarily but an estimate. It is not possible to know precisely the effect that any given rate, or change from a prevailing rate, will have upon revenues (and therefore upon the LEC's rate of return); that depends upon the elasticity of the demand for the service, which cannot be known for certain, 1 ALFRED E. KAHN, THE ECONOMICS OF REGULATION: PRINCIPLES AND INSTITUTIONS 185-88 (1970); *see also* Douglas H. Ginsburg, *The Goals of Antitrust Revisited,* 147 J. INST'L & THEORETICAL ECON. 24, 25 (1991). If demand is at all price-elastic, however, then it

is axiomatic that a reduction in the price charged will result in an increase in the quantity sold and that any reduction in revenues associated with the reduction in price will be less than proportionate. *See* WILLIAM J. BAUMOL & ALAN S. BLINDER, ECONOMICS: PRINCIPLES AND POLICY 468-72 (5th ed. 1991). Nonetheless, the approach that the IXCs have taken to calculating damages is premised upon a model in which it is assumed that demand is completely inelastic over the relevant range (and that short-run marginal cost is zero), so that a one percent reduction in rates would have produced a full one percent reduction in revenues. In other words, it establishes as "reasonable" the rate that would have produced earnings within the prescribed level, holding cost and demand constant. This approach yields a conservative estimate because it implicitly assumes that the quantity demanded would not increase if the price were lowered. The actual reasonable rate would, if anything, therefore be lower than the rate derived by the IXCs.

Because any determination of the reasonable rate will necessarily be an estimate under the rate-of-return regime, and because the estimate relied upon by the IXCs is a conservative one, we reject the LECs' contention that the Commission failed to require the IXCs adequately to prove their damages.

4. *The statute of limitations*

The Communications Act provides that "[a]ll complaints against carriers for the recovery of damages not based on [charges in excess of those made applicable in a tariff] shall be filed with the Commission within two years from the time the cause of action accrues, and not after." 47 U.S.C. § 415(b). The question here is at what point an IXC's cause of action accrues. The LECs argue for what amounts to a "time-of-injury" rule; they contend that a cause of action accrues on the last day of the monitoring period to which it relates—which would

mean that nearly all of the claims at issue here are time-barred. The Commission, on the other hand, argues for what is generally called a "discovery-of-injury" rule; it contends that a cause of action accrues only when the IXC discovers (or with due diligence should discover) that it has been overcharged. According to the Commission, moreover, that does not occur until after the LEC files its final earnings report for the two-year monitoring period at issue. We agree with the Commission that the discovery-of-injury rule applies to these causes of action.

In *Connors v. Hallmark & Son Coal Co.*, 935 F.2d 336, 342 (D.C.Cir.1991), the court (per then-Judge Ruth Bader Ginsburg) aligned the law of this circuit with that of the eight other circuits to have considered the matter and held that "the discovery[-of-injury] rule is the general accrual rule in federal courts," applicable in federal question cases "in the absence of a contrary directive from Congress." We also explained that the time-of-injury rule is not inconsistent with, and indeed should be considered a part of, the broader discovery-of-injury rule:

> [I]f the injury is such that it should reasonably be discovered at the time it occurs, then the plaintiff should be charged with discovery of the injury, and the limitations period should commence, at that time. But if, on the other hand, the injury is not of the sort that can readily be discovered when it occurs, then the action will accrue, and the limitations period commenced, only when the plaintiff has discovered, or with due diligence should have discovered, the injury.

The LECs point to no directive from the Congress suggesting that the general discovery-of-injury rule does not apply to a damage claim asserted under § 206 of the Communications Act. Instead, they rely only upon our recent decision in *3M Co. v. Browner*, 17 F.3d 1453

(1994), which involved a civil enforcement proceeding brought for violations of the Toxic Substances Control Act that were alleged to have occurred more than five years earlier. We held that the EPA's cause of action accrued, and thus the five-year statute of limitations began to run, when the violation occurred rather than when the EPA actually discovered or with due diligence should have discovered the violation. *Id.* at 1460-63. In so doing, we specifically took note of the general discovery-of-injury rule that we had recently adopted in *Connors*, but explained that it "applied only to remedial, civil claims." *Id.* at 1460. Because the case against 3M was penal in nature—the statute imposed a five-year limitations period for any "fine, penalty, or forfeiture"—we held that the generally applicable discovery-of-injury rule adopted in *Connors* did not apply in that case. If the discovery-of-injury rule were applicable to an agency-initiated civil penalty case, then the court would have to determine whether the agency, with the exercise of due diligence should have detected the violations earlier than it had—an oversight activity that (at least absent a statutory directive to the contrary) is better suited to the legislature than to the court. *Id.* at 1461.

As the foregoing suggests, *3M* is of no help to the LECs' cause because it deals only with the special circumstance, not present here, of an agency-initiated civil penalty case; *3M* leaves the discovery rule of *Connors* intact for remedial civil actions such as the IXCs brought against the LECs. Therefore we follow the discovery-of-injury rule adopted in *Connors* to determine when the claims of the IXCs accrued.

The LECs contend that even if the discovery-of-injury rule applies, most of the IXCs' claims are time-barred: The Commission allowed them to go forward, according to the LECs, only because it erroneously held that an IXC's claim does not accrue until the LEC from which the IXC seeks damages files its final earnings report for

the monitoring period at issue, *i.e.*, nine months after the close of that period. The LECs argue that such a claim accrues three months after the close of the monitoring period, the time by which the Commission requires the LEC to file a preliminary earnings report.

The LECs' position would be tenable if, after reviewing the relevant preliminary reports, an IXC exercising due diligence should have discovered that it had been over-charged. *Connors,* 935 F.2d at 342. But that is not the case. The *raison d'etre* for the final report is to afford the LEC time to adjust the data submitted in its preliminary report, *see Amendment of Part 65, Interstate Rate of Return Prescription: Procedures and Methodologies to Establish Reporting Requirements, Report and Order,* CC Docket No. 86-127, 1 F.C.C.R. 952, 954 (1986); it therefore would be passing strange to require an IXC to assume that the preliminary report is a reliable indicator of whether the LEC has earned more than allowed. Indeed, the Commission points out that in five of the claims before us the preliminary report did not accurately reveal whether the LEC had exceeded its allowable rate of return. This, we think, is convincing evidence that even a diligent IXC could not reliably ascertain whether it had been injured solely upon the basis of the preliminary report. Therefore we agree with the Commission that a cause of action for damages pursuant to § 206 does not accrue until after the LEC files its final report.

B. *The IXCs' Claims*

Recall that the IXCs ask us to vacate only the Commission's "limited offset" rule, that is, its policy of allowing a LEC to offset against any overcharge that an IXC paid for one type of access the amount that the same IXC "underpaid" the LEC (*i.e.*, insofar as it paid a rate that yielded a return less than the prescribed maximum) for any other type of access during the same monitoring period. The IXCs advance three primary contentions:

They claim that allowing "limited offsets" (1) violates both FCC and related ICC precedent, and (2) the "filed rate doctrine"; and (3) was inadequately explained (and thus arbitrary and capricious) under the standards of the Administrative Procedure Act. Because we agree with the IXCs' first contention and upon that basis vacate the limited offsets, we do not reach the latter two claims. (Nor do we consider Allnet's alternative claim that the Commission improperly set the interest rate it is due on its award of damages.)

In *Laning-Harris Coal & Grain Co. v. St. Louis & San Francisco Ry. Co.*, 15 I.C.C. 37 (1909), a customer complained before the ICC that the defendant railroad had overcharged it by $42 on shipments made during the period 1906-07. "In answer to the complaint defendant admitted that it is indebted to complainant in said sum, but shows that in 1902 and 1903 it undercharged the complainant the sum of $109.50 [and] therefore claims set-off and asks dismissal of the complaint." *Id.* at 38. The Commission denied the set-off, explaining that:

> It is clear that the Commission . . . is not authorized to adjudicate the claim of a railroad company against a shipper, but only the claim of a shipper against a railroad company. . . . To award set-off amounts to the same thing as adjudicating the claim of the railroad company against the shipper, and entry of an order based upon a set-off could occur only after such adjudication. Plainly, if the Commission is without authority to determine the rights of the parties, it is also powerless to enter an order based upon a determination of those rights.

Because the Congress borrowed heavily from the Interstate Commerce Act when it drafted the Communications Act of 1934—indeed the damage sections upon which the IXCs base their claims are derived from the ICA—both this court and the Commission often turn to decisions

under the ICA for guidance in interpreting the Communications Act. *See, e.g., American Broadcasting Cos. v. F.C.C.*, 643 F.2d 818, 820-21 (D.C.Cir.1980); *MCI Telecommunications Corp. v. AT & T*, 85 F.C.C.2d 994, 998 (1981). It is not surprising, therefore, that the Commission has expressly adopted the rule of *Laning-Harris. See Thornell Barnes Co. v. Illinois Bell Telephone Co., Decision*, Docket No. 14645, 1 F.C.C.2d 1247 (1965).

The customer in *Thornell Barnes* was seeking damages upon the ground that Illinois Bell had improperly charged him for misdirected calls. After calculating the customer's damages, the Commission stated:

> We do not believe . . . that it would be proper to "set off" against this amount the amount that Barnes was undercharged on certain calls at the station-to-station rate because this would involve a determination of the carrier's rights against a subscriber, over which this Commission has no jurisdiction. See *Laning-Harris Coal & Grain Co. v. St. L. & S.F. R.R. Co.*, 15 ICC 37 (1908).

Id. at 1275. The IXCs argue that both the ICC's decision in *Laning-Harris* and the FCC's decision in *Thornell Barnes* preclude the Commission from awarding the LECs limited offsets in the present cases. That, they contend, would "involve a determination of the carrier's rights against a [customer], over which this Commission has no jurisdiction."

The Commission attempts to distinguish *Thornell Barnes* on the ground that it involved a claim for "set-off" while the instant cases involve claims for "offsets." Truly; it explains that a set-off "involves the adjudication of a claim separate from the one advanced by the plaintiff" and argues that it "did not adjudicate, through the use of offsets or otherwise, any claims of any LEC against any customer." Rather, the Commission argues, it considered the

offsets only in the course of determining the damages that the complainants actually incurred. That is appropriate, according to the Commission, because the "focus of [the IXCs'] complaints is not [the LECs'] individual interstate access rates *per se*, but the excessive earning produced by these rates and their effect on [the IXCs]." *MCI Damages Order*, 8 F.C.C.R. at 1527. We are not persuaded by the Commission's attempted distinction.

First, while one may be able to construct a distinction between set-offs and offsets, *but see Steinmeyer v. Warner Consolidated Corp.*, 42 Cal.App.3d 515, 116 Cal.Rptr. 57, 59-60 (1974) (using the two terms interchangeably), the Commission itself blurred the line between the two (if two they be) in *Thornell Barnes*. Although the Commission there characterized the claim made by the carrier as a "set-off," it considered the claim only as part of its damage calculation. The Commission thus appears to have considered, and rejected as *ultra vires*, the very manner of proceeding that it now repackages and embraces as an offset, *viz.*, folding the carrier's undercharge for one service into its evaluation of the actual damage that the customer suffered by reason of being overcharged for another. The new approach is inconsistent not only with the Commission's own precedent but also with the course that the ICC took in the aftermath of *Laning-Harris*. In *Breece Veneer Co. v. Chesapeake & Ohio Ry. Co.*, 182 I.C.C. 690 (1932), the ICC awarded a customer reparations in the amount it was overcharged on certain shipments even as it refused to consider that the customer had not paid the carrier at all for a different shipment of the same commodity. The ICC did not accept the contention (adopted by a lone dissenter) that the strictures of *Laning-Harris* could be avoided simply by reducing the damages that the customer receives upon its claim against the carrier by the amount of the carrier's claim against the customer. *Id.* at 692. In short, the Commission's attempt to justify its allowance of offsets here is contrary

both to its own precedent and to the ICC's longstanding interpretation of the cognate provisions of the ICA.

But there is another problem with the Commission's approach: The award of an offset amounts to an implicit determination that the defendant LEC was entitled to earn more than the amount that it actually earned from the rates that it charged. Under the rate-of-return regime as the Commission promulgated it, however, a LEC enjoys no such entitlement, either for interstate access overall or for any individual type of access. Indeed in *NETCO* we noted with approval that the Commission had "declined to set minimum guaranteed rates of return for carriers," 826 F.2d at 1108-09, and nothing of which we are aware in any subsequent rulemaking proceeding suggests that the Commission has since changed course. The Commission may not now, in adjudicating an individual damage complaint, simply manufacture out of whole cloth such a minimum guarantee—here a guarantee that the LEC will earn for the offsetting service a rate of return no lower than the rate of return actually obtained plus the additional amount (up to the maximum allowed) necessary to offset overearnings on the service for which the IXC has made the claim to be offset.

The Commission attempts to justify this departure from its own regulatory scheme by explaining that "it is reasonable to inquire into [IXC's] overall purchase of interstate access services" because the "focus of [each IXC's] complaints is not [the LECs'] individual interstate access rates *per se*, but the excessive earnings produced by these rates and their effect on [that IXC]." *MCI Damages Order*, 8 F.C.C.R. at 1527. That explanation begs the question whether "excessive earnings" from the provision of one service can be offset by earnings foregone in the provision of another service. Most of the IXCs' claims are category-specific; that is, they are not based upon the rate of return that the LEC earned overall from the provision of interstate access services but rather upon the

rate of return that the LEC earned from the provision of a particular type of access service. The IXCs seek to recover money from the LECs for having done the very thing that the Commission, in setting category-specific rate-of-return prescriptions, sought to prohibit—namely, earning more than the maximum allowed from the provision of a particular service. The Commission cannot avoid the inconsistency between the regulatory scheme that it devised and its more recent implementation of that scheme by blaming the IXC for the manner in which it brought its claim, *i.e.*, for focusing upon the LEC's excessive earnings rather than the specific rate that it charged.

Finally, the Commission's approach to offsets is inconsistent with the statutory and regulatory goal of preventing discrimination in the pricing of access services. *See Prescription Reconsideration*, 59 Rad.Reg.2d at 1603 justifying category-specific rate-of-return prescriptions on ground that Commission is "bound by the Communications Act to ensure that rates . . . do not produce unreasonable discrimination or undue preferences"; 47 U.S.C. § 202 ("It shall be unlawful for any common carrier to make any unjust or unreasonable discrimination in charges"). By awarding an offset in favor of a LEC the Commission effectively allows the complaining IXC alone to be charged for the offsetting category of service at a rate above what others paid for it, up to the rate that would yield the maximum rate of return for that type of service. An IXC that cannot or does not bring a refund claim in connection with its purchase of an overearning access service (X) will therefore pay less for the underearning category of service (Y) than will the IXC that does bring a successful refund claim. The Commission offers no convincing explanation of why an IXC that purchased little or none of the service (X) for which the LEC overearned (and hence did not bring an overcharge claim) should enjoy the low rate that the LEC charged for a service (such as Y) in which it underearned while an IXC that purchased more of the overpriced service should not.

In sum, by factoring into its damage calculation the complaining IXC's so-called "underpayments" for other categories of service, the Commission effectively adjudicates the defending LEC's claim for underearnings, in derogation of (1) FCC and related ICC precedent; (2) the Commission's rate-of-return regulatory regime, under which a LEC is not entitled to any minimum rate of return; and (3) the statutory and regulatory norms against rate discrimination. For all these reasons, we hold that the Commission's limited offset policy cannot stand.

III. CONCLUSION

In summary, we deny the consolidated petitions of the LECs and the petition of Cincinnati Bell, and grant the consolidated petitions of the IXCs. The Commission's orders are therefore affirmed except to the extent that they involve limited offsets, as to which we vacate the Commission's orders and remand these matters for the Commission to recalculate the complainants' damages. We dismiss Allnet's petition as moot in view of our decision invalidating limited offsets.

So ordered.

APPENDIX B

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

File No. E-88-44

In the Matter of
MCI TELECOMMUNICATIONS CORPORATION,
Complainant,
v.

PACIFIC NORTHWEST BELL TELEPHONE COMPANY,
Defendant;

File No. E-88-46

MCI TELECOMMUNICATIONS CORPORATION,
Complainant,
v.

PACIFIC BELL TELEPHONE COMPANY,
Defendant;

File No. E-88-47

MCI TELECOMMUNICATIONS CORPORATION,
Complainant,
v.

SOUTHWESTERN BELL TELEPHONE COMPANY,
Defendant;

File No. E-88-48

MCI TELECOMMUNICATIONS CORPORATION,
Complainant,

v.

WISCONSIN BELL, INC.,
Defendant;

File No. E-88-49

MCI TELECOMMUNICATIONS CORPORATION,
Complainant,

v.

THE CHESAPEAKE & POTOMAC TELEPHONE COMPANIES,
Defendants;

File No. E-88-50

MCI TELECOMMUNICATIONS CORPORATION,
Complainant,

v.

NEW JERSEY BELL TELEPHONE COMPANY,
Defendant;

File No. E-88-51

MCI TELECOMMUNICATIONS CORPORATION,
Complainant,

v.

MOUNTAIN STATES TELEPHONE & TELEGRAPH COMPANY,
Defendant;

File No. E-88-52

MCI TELECOMMUNICATIONS CORPORATION,
Complainant,

v.

MICHIGAN BELL TELEPHONE COMPANY,
Defendant;

File No. E-88-54

MCI TELECOMMUNICATIONS CORPORATION,
Complainant,

v.

NORTHWESTERN BELL TELEPHONE COMPANY,
Defendant;

and

File No. E-88-55

MCI TELECOMMUNICATIONS CORPORATION,
Complainant,

v.

THE DIAMOND STATE TELEPHONE COMPANY,
Defendant.

MEMORANDUM OPINION AND ORDER

Adopted: December 12, 1989;

Released: January 9, 1990

By the Commission:

I. INTRODUCTION

1. The primary question presented in these consolidated proceedings is whether a complainant/customer has a right under the Communications Act to recover damages if the complainant can establish that a carrier from whom it has purchased service has violated a valid rate of return prescription. We answer that question in the affirmative.

2. Complainant MCI alleges that the above-noted defendants earned in excess of the rate of return prescribed by the Commission for the period from October 1, 1985 through December 31, 1986; thus, MCI contends, the defendants' rates were in violation of the prescription order and were unjust and unreasonable. MCI claims it took interstate access service during this period from the defendants, paid the tariffed charges for such service, was damaged as a result, and, therefore, is entitled to reparations. We conclude that MCI has met its burden of establishing that the defendants violated the Act and are liable to MCI to the extent it can establish that it was damaged as a result of these violations.

3. We begin with an account of the applicable statutory scheme and a brief overview of certain Commission orders and court decisions that preceded the filing of MCI's complaints.

II. BACKGROUND

4. The Communications Act of 1934 (the Act) grants the Commission a mandate to regulate "so as to make available . . . efficient, Nation-wide, . . . communications service, with adequate facilities at reasonable charges. . . ."[1] Title II of the Act requires that carriers' rates for communications services must be just, reasonable, and non-discriminatory.[2]

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[1] 47 U.S.C. § 151 (1982).

[2] 47 U.S.C. § 201(b), 202(a) (1982).

5. The Act provides the Commission with various tools to fulfill its regulatory functions. Some of these tools give us the means to affect rates indirectly, such as by prescribing a carrier's accounting system and depreciation rates,[3] or controlling its entry into or exit from the interstate market.[4] Other provisions of the Act are connected more directly with the ratemaking process. Section 203 authorizes us to determine the information that must accompany a carrier's tariff filings, while Section 204 empowers us to investigate the lawfulness of proposed rates and, pending hearing, suspend the effectiveness of those rates for up to five months.[5] Section 205 of the Act also grants us the authority, after a full opportunity for hearing, "to determine and prescribe" just and reasonable rates or practices "to be thereafter observed."[6]

6. The statute provides the Commission broad authority to effectuate its provisions and to penalize those who violate them. Section 4(i) states that the Commission "may perform any and all acts, make such rules and regulations, and issue such orders, not inconsistent with [the Act], as may be necessary in the execution of its functions."[7] Title V contains provisions authorizing the levying of fines and forfeitures.[8]

7. The Act also expressly provides private parties a right to file a complaint against carriers and obtain reparations if the party can establish that a carrier has violated the Act and the party has been damaged as a result of such violation. Specifically, the Act states that "any person" may petition the Commission in complaint

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[3] 47 U.S.C. §§ 220 (1982).

[4] 47 U.S.C. § 214 (1982).

[5] 47 U.S.C. §§ 203-204 (1982).

[6] 47 U.S.C. § 205(a) (1982).

[7] 47 U.S.C. § 154(i) (1982).

[8] 47 U.S.C. § 501 *et seq.* (1982).

of "anything done or omitted to be done" by any carrier in contravention of the Act, and that carriers shall be liable "for the full amount of damages sustained in consequence of any such violation." The Commission has a duty to investigate a complaint "in such manner and by such means as it shall deem proper." If the Commission finds that the complainant is entitled to an award of damages, the Commission has authority to order the carrier to pay the complaining party the sum to which it is entitled.[9]

8. In 1972, the Commission, in an effort to carry out its responsibilities in a more effective and expeditious manner, asserted the authority to prescribe the rate of return a carrier may earn. That authority was upheld in 1975 by the U.S. Court of Appeals for the District of Columbia Circuit and has not been questioned elsewhere.[10]

9. Prior to 1984, the Commission exercised this authority to prescribe a rate of return for a single entity: the Bell System.[11] As a result of the telecommunications industry's structure at that time, the regulatory effect of this single prescription rippled throughout the industry as a whole.[12] The subsequent Bell System divestiture and

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[9] 47 U.S.C. §§ 206, 208-209 (1982).

[10] *Nader v. FCC*, 520 F.2d 182, 203-204 (D.C. Cir. 1975). *See United States v. FCC*, 707 F.2d 610 (D.C. Cir. 1983). The D.C. Circuit ruled that such rate of return prescriptions are "necessary for the Commission to carry out its [ratemaking] functions in an expeditious manner." *Nader v. FCC*, 520 F.2d at 204.

[11] On one occasion during this period, AT&T's earnings exceeded the return established by the Commission for determining compliance with our prescription. The Commission's order directing AT&T to refund its overearnings was upheld by the U.S. Court of Appeals for the District of Columbia Circuit. *See New England Telephone and Telegraph Co. v. FCC*, 826 F.2d 1101 (D.C. Cir. 1987) (*New England Telephone*), *cert. denied*, 109 S. Ct. 1942 (1989).

[12] Although the Commission prescribed a rate of return for the Bell System alone and not for so-called "independent" (*i.e.*,

the concurrent development of the access charge system altered the industry's structure fundamentally,[18] and created the prospect of having to prescribe a rate of return not just for a single entity, but for all eight entities that emerged after divestiture (*i.e.*, AT&T and the seven Re-

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non-Bell) local exchange carriers, the return prescribed for the Bell System operated indirectly as a check on the justness and reasonableness of all local exchange carrier earnings because of the existence of a process known as "settlement and division of revenues." Essentially, this process entailed the pooling of costs and revenues among the Bell System companies and, separately, between them and the independents. The process was referred to as a "partnership" because it helped all the participants achieve a relatively stable and uniform return on their investment. For a more complete discussion of the "partnership" process and its impact on the industry, see *MTS and WATS Market Structure, Second Supplemental Notice of Inquiry and Proposed Rule Making*, 77 FCC 2d 224, 226-231 (1980); *MTS and WATS Market Structure, Amendment of Part 67 of the Commission's Rules and Establishment of a Federal-State Joint Board, Recommended Decision and Order*, 2 FCC Rcd. 2324, 2337-2340 (1987).

[18] The Commission has prescribed for all local exchange carriers, including the defendants, a methodology known as the "access charge system," which carriers are required to follow in tariffing their interstate services. The system determines, *inter alia*, the carriers' overall rate structure and the allocation of costs within that structure, and was in effect during the period covered by the complaints. The access charge system is codified in Part 69 of the Commission's rules. *See* 47 C.F.R. § 69.1 *et seq.* (1988). These rules were developed in a proceeding that was the subject of numerous challenges on appeal. With a few exceptions not relevant to the instant complaint proceedings, these appeals were denied by the D.C. Circuit. *See NARUC v. FCC*, 737 F.2d 1095 (D.C. Cir. 1984), *cert. denied*, 469 U.S. 1227 (1985). During the access charge Rule Making, the Commission terminated the "settlements and division of revenues" agreements because the "partnership," as it was then structured, was incongruent with the rapidly changing industry structure. It was replaced by more limited pooling arrangements, within the access charge framework, in which only local exchange carriers participated. *MTS and WATS Market Structure, Third Report and Order*, CC Docket No. 78-72, 93 FCC 2d 241, 326-330 (1983).

gional Bell Holding Companies) and approximately 1400 other local exchange carriers as well.

10. Faced with this prospect, the Commission adopted, in a broad Rule Making proceeding: (1) methodologies to be used to prescribe maximum rates of return for AT&T and local exchange carriers; (2) procedures for represcribing rates of return on a regular basis; (3) a system of monitoring carriers' earnings; and (4) a requirement that overearnings be refunded, either directly to those who had paid rates that produced the overearnings, or pursuant to automatic, prospective adjustments to tariff rates.[14] In keeping with its traditional approach to prescribing rates of return, the Commission established both an authorized return and a "spread" or "buffer" above that return for use in proceedings relating to the enforcement of the prescription. In other words, the authorized return would be employed in computing tariff rates; the spread, or buffer, would be used in combination with the authorized return "to determine whether a rate of return prescription has been violated."[15] The Commission also defined particular time periods for measuring compliance with the prescribed return. Consistent with its traditional practice, the Commission did not prescribe a minimum rate of return.[16]

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[14] *See Authorized Rates of Return for the Interstate Services of AT & T Communications and Exchange Telephone Carriers,* FCC 85-527 (released Sept. 30, 1985), 50 Fed. Reg. 41350 (Oct. 10, 1985). (*Phase I Order*), *on reconsideration, Memorandum Opinion and Order,* FCC 86-114 (released March 24, 1986), 51 Fed. Reg. 1103 (Apr. 1, 1986) (*Phase I Reconsideration*); *on further reconsideration,* 2 FCC Rcd 190 (1987). *See also Procedures and Methodologies to Establish Reporting Requirements,* CC Docket No. 86-127, FCC 86-514 (released Dec. 3, 1986), 52 Fed. Reg. 273 (Jan. 5, 1987).

[15] *Phase I Order,* 50 Fed. Reg. at 41353.

[16] *See, e.g., Phase I Order,* 51 Fed. Reg. at 41350, para. 1 ("in this phase of the proceeding, we address the maximum allowable rates of return and enforcement procedures for the regulated . . . interstate access services of local exchange carriers (LECs)"); *Id.,*

11. The Commission determined that it would review earnings on an overall basis, and on three categories of access charge rate elements: special, common line, and switched traffic sensitive. The Commission acknowledged that reviewing earnings in this manner might require a carrier to refund excessive earnings in one category even though its overall return was not excessive. The Commission determined, however, that such a review would not be unfair to carriers because of the safeguards built into its plan. The safeguards included a long evaluation period, the aggregation of access elements into three categories, the freedom afforded carriers to select the geographic level at which their rates would be tariffed, and the creation of the "spread" or "buffer" above the authorized return. The Commission noted that each of these safeguards would provide carriers flexibility to offset earnings "peaks" and "valleys," and thereby provide them a reasonable opportunity to achieve their allowed return.[17]

12. Reviewing earnings on a categorical basis also furthered the public interest, the Commission determined, by helping to prevent discrimination among the users of access services.[18] The Commission stated:

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51 Fed. Reg. at 41352, para. 22 (Commission affirms decision tentatively adopted at earlier stage of proceeding that it "should not prescribe a minimum return requirement"); *see also New England Telephone*, 826 F.2d at 1108 (noting the Commission's practice not to set minimum guaranteed rates of return); *but cf. AT & T v. FCC, infra* n.23, 836 F.2d at 1390 (expressing the belief that the return prescribed by the Commission is the minimum possible return; it is both the "minimum and maximum").

[17] *Phase I Order*, 50 Fed. Reg. at 41352-53 (paras. 13-21).

[18] *Id.* 50 Fed. Reg. at 41352 (para. 16). The foremost goal of the Commission's access charge proceeding was to prevent discrimination by establishing a single, uniform and nondiscriminatory tariff structure covering those services that make identical or similar use of local exchange carrier facilities. *See MTS and WATS Market Structure, Third Report and Order*, CC Docket No. 78-72, 93 FCC 2d 241 (1983).

> Our obligation is to provide carriers a reasonable opportunity to achieve their authorized return. That opportunity, however, is not unlimited; we are bound by the Communications Act to ensure that rates are just and reasonable, and do not produce unreasonable discrimination or undue preferences. [Reviewing earnings on a categorical basis helps] to accomplish that goal by not allowing a carrier to offset excessive rates to one customer with deficient rates to another. A carrier is still afforded the opportunity to achieve its overall return, it simply must do so in a non-discriminatory manner.[19]

13. During the 15 month time period at issue in the instant complaints, local exchange carriers, including the defendants, were required to file rates calculated to earn a 12.75 percent return.[20] Because the initial review period would be 15 months, rather than two years, as would be followed thereafter, the Commission expanded the "buffer" that would be used during this initial period to determine whether the prescription had been violated.[21] Thus, car-

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[19] *Phase I Reconsideration*, 51 Fed. Reg. at 1105 (para. 34).

[20] The 12.75 percent rate of return was prescribed by the Commission in 1981 for the unified Bell System. *AT & T Co.* 86 FCC 2d 221, 251 (1981). In reviewing this prescription on appeal, the District of Columbia Circuit held that the Commission had acted reasonably in selecting a return within a zone of reasonableness. *See United States v. FCC*, 707 F.2d 610, 615-619 (1983). Following divestiture, the Commission, pursuant to notice and comment Rule Making procedures, directed AT&T and the BOCs to target their rates to achieve a 12.75 percent return. *See MTS & WATS Market Structure*, 93 FCC 2d 241, 315-316 (1983). In the rate of return proceedings, the Commission determined, based on its review of the record, that the 1981 prescription would continue in force for an interim period (*e.g.*, until the Rule Making was completed and the methodologies and procedures adopted therein were available for prescribing a new rate of return). *Phase I Order*, 50 Fed. Reg. at 41350 (para. 4).

[21] *Phase I Order*, 50 Fed. Reg. at 41352 (para. 21). The initial review period was shortened in order to align it with the "test

riers were given notice that a 13.10 percent level of earnings would be the maximum allowable rate of return on overall interstate earnings during this period and 13.25 percent would be the maximum allowable rate of return for any access service category.[22]

14. In January 1988, the U.S. Court of Appeals for the District of Columbia Circuit set aside the automatic refund mechanism as arbitrary and capricious "because it is inconsistent with the rate of return prescription it purports to enforce." [23] The court acknowledged, however, that "the Commission has authority under the Act to order refunds where a carrier has violated an outstanding rate-of-return prescription." [24]

15. Against this background, we turn to the pleadings of the parties.

III. PLEADINGS OF THE PARTIES

16. In February 1988, MCI Telecommunications Corporation (MCI) filed ten formal complaints [25] against the defendant local exchange carriers.[26] MCI alleges that the

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year" used by the carriers to develop their rates. *Id.* (para. 21 & n.26).

[22] 47 C.F.R. § 65.701(b) (1988).

[23] *AT & T v. FCC*, 836 F.2d 1386, 1390 (D.C. Cir. 1988).

[24] *Id.*, 836 F.2d at 1392.

[25] Due to the similarity of the issues and arguments raised by the parties, the complaints have been consolidated for disposition.

[26] The defendants are: Pacific Bell Telephone Company (Pacific Bell); Southwestern Bell Telephone Company (SWB); Wisconsin Bell, Inc. (Wisconsin Bell); The Chesapeake & Potomac Telephone Companies (C&P); New Jersey Bell Telephone Company (New Jersey Bell); Michigan Bell Telephone Company (Michigan Bell); The Diamond State Telephone Company (Diamond State); Mountain States Telephone & Telegraph Company (Mountain States); Pacific Northwest Bell Telephone Company (PNB); and Northwestern Bell Telephone Company (NWB). For the convenience of the reader, we occasionally refer to the last three listed defendants as US West or the US West Carriers.

rates it paid for certain of the defendants' interstate access services during the period from October 1, 1985 through December 31, 1986 were unjust and unreasonable in violation of Section 201(b) of the Act. 47 U.S.C. § 201(b). MCI supported its allegations with evidence in the form of reports filed with this Commission by the defendants for the 15 month period at issue which show that the defendants achieved earnings in excess of this Commission's prescribed rate of return on one or more of the three interstate access service categories established for purposes of enforcing that prescription.[27]

17. Pursuant to Sections 206 through 209 of the Act, MCI requests that this Commission declare the defend-

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[27] The interstate access categories are carrier common line, special, and switched traffic sensitive. *See* 47 C.F.R. § 65.702 (1988). The monitoring reports recite that for the period October 1, 1985 through December 31, 1986: Pacific Northwest Bell earned returns in the special access category of 15.09 percent in the State of Idaho and earned returns in the switched traffic sensitive access category of 14.76 percent in Oregon; Pacific Bell earned a return of 14.51 percent in the switched access category; Southwestern Bell earned returns in the special access category of 15.43 percent in Missouri and 15.99 percent in Oklahoma and earned returns in the switched access category of 14.21 percent in Arkansas, 16.21 percent in Kansas and 14.93 percent in Missouri; Wisconsin Bell earned a return of 16.66 percent in the switched access category; Michigan Bell earned a return of 13.37 percent in the switched access category; C&P earned a return of 13.38 percent in the switched access category; New Jersey Bell earned a return of 14.74 percent in the switched access category; Mountain States earned returns in the switched access category of 14.60 percent in Arizona, 15.81 percent in Idaho, 15.20 percent in Montana, 14.97 percent in New Mexico, 13.67 percent in Utah and 14.93 percent in Wyoming; Diamond State earned a return of 15.65 percent in the special access category; and Northwestern Bell earned returns in the special access category of 14.31 percent in Iowa, 13.85 percent in Minnesota, 13.63 percent in Nebraska and 16.01 percent in North Dakota and earned returns in the switched access category of 14.64 percent in Iowa, 14.44 percent in Minnesota, 15.79 percent in Nebraska and 19.71 percent in North Dakota.

ants' charges for the period from October 1, 1985 through December 31, 1986 to be in violation of the rate of return prescription and Section 201(b) of the Act, and order the defendants to pay damages to MCI equal to the difference between the amount it actually paid for interstate access service during that period and the amount it would have paid if the charges had earned no more than the maximum allowable rate of return, plus interest on this amount from January 1, 1987 at the rate specified by the Commission in the Docket 84-800 proceeding. At the time MCI filed its complaints, it stated that the precise amount of damages it suffered could not be determined, and it alleged a right under Section 1.723(b) of the Rules to file a supplemental complaint on which damages may be awarded.[28]

18. All of the defendants filed answers and motions to dismiss the complaints. Mountain States, NWB and PNB (referred to collectively herein as "US West" or the "US West carriers") jointly filed an answer and motion to dismiss in which they claim that MCI has not stated a cause of action upon which relief may be granted. The US West carriers admit they filed monitoring reports and admit to the specific recitations of the earned interstate rates of return cited by MCI, but also state that they underearned as to specific access elements. They further contend that the earned rate of return on a particular element does not establish the justness or reasonableness of the underlying rate. The US West carriers allege that MCI's claim for damages is nothing more than a claim for

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[28] At the time the complaints were filed, Section 1.723(b) provided that "Damages will not be awarded upon a complaint unless specifically requested. Damages may be awarded, however, upon a supplemental complaint based upon the finding of the Commission in the original proceeding." That section has since been revised and renumbered, but continues to provide for the filing of supplemental complaints. *Compare* 47 C.F.R. 1.723(b) (1987) *with* 47 C.F.R. 1.722(b) (1988).

automatic refunds, the same as that invalidated by the Court of Appeals for the District of Columbia in *AT & T v. FCC*. They argue that neither *New England Telephone* nor *AT & T v. FCC* stands for the proposition that exceeding a rate of return provides a carrier with a cause of action for damages. Finally, the US West carriers state that a portion of the claim is barred by the statute of limitations, 47 U.S.C. § 415. To the extent that the Commission upholds MCI's complaint, defendants claim in a contingent cross complaint that they are entitled to sums for those access elements on which they underearned.

19. In its answer and motion to dismiss, Pacific Bell denies that its rates were unlawful and denies that MCI was damaged. Pacific Bell claims that to award MCI the damages it seeks would violate the Act because MCI would be paying less than Pacific Bell's tariffed rate. It further contends that Docket 84-800 did not establish a private cause of action that would permit individual remedy and that it would be premature to consider an individual complaint for alleged damages because of the court remand in *AT & T v. FCC*. Pacific Bell argues that part of the claim is barred by the statute of limitations and that, for a portion of the period, the rates charged were not unlawful because it earned less than the authorized rate of return.

20. SWB also argues that MCI has failed to state a cause of action. It argues that the complaint is based on the automatic refund rule that was invalidated in *AT & T v. FCC* and that it is barred, in part, by the statute of limitations. SWB contends that MCI alleges only that SWB realized returns for particular categories of interstate access service in particular states but does not allege that SWB overearned overall and, therefore, that MCI's complaint should be dismissed.

21. Wisconsin Bell's and Michigan Bell's answers and motions to dismiss were identical in their essentials. They

admit that the Commission prescribed a maximum overall return but deny that the Commission's "prescription" for access categories has any lawful effect. To the extent the claim is for special access, Wisconsin Bell states that MCI only paid a portion of the special access tariff rate. They deny that they "actually earned" the amount recited in the monitoring reports because, they contend, the methodology they used to compute their reported earnings overstates the return on interstate switched access. Wisconsin Bell and Michigan Bell argue that the rates were not carrier-initiated and that, in any event, damages in this case could only be awarded prospectively from the date the complaint was filed. They argue further that the claim is barred by the statute of limitations. The defendants also contend that if any damages were suffered, it was by MCI's customers, not MCI, and thus any refunds must be flowed-through to those customers.

22. C&P, New Jersey Bell and Diamond State filed a consolidated answer and motion to dismiss. They argue that the complaint fails to state a cause of action because MCI alleges only that the defendants reported overearnings in access categories and not overall. They contend that *AT & T v. FCC* bars MCI's claim and, therefore, it should be dismissed.

23. MCI filed replies to the answers and oppositions to the motions to dismiss. In response to the defendants' contention that the complaints are legally deficient because MCI fails to demonstrate that the tariffed charges paid by MCI were unjust and unreasonable, MCI contends that the effort by the defendants to divorce the earned rate of return from the lawfulness of the carriers' rates ignores the history and purpose of rate of return regulation. MCI further states that the court in *AT&T v. FCC* invalidated the Commission's automatic refund scheme, but left undisturbed the Commission's authority to establish an allowable maximum rate of return on interstate access. MCI also disagrees with the defendants'

claims that the complaints are barred by the statute of limitations, arguing that the cause of action accrues when information that the actual return exceeded the authorized rate became publicly available, in this case with the filing of the monitoring reports on September 30, 1987. It also claims that the defendants' contingent cross complaints are unauthorized and should be stricken from the record.

24. On July 27, 1989, the Common Carrier Bureau (Bureau) issued "Orders to Show Cause" to each of the defendants directing them to show cause why the Commission should not order the payment of damages sought by the complainant.[20] The Bureau found defendants' reliance on *AT & T v. FCC* in their answers and motions to dismiss to be unfounded, stating that the court in that case did not discuss Section 208 complaint proceedings, nor did it alter the statutory scheme of the Communications Act or limit the remedies Congress established therein. The Bureau noted that the Communications Act provided MCI the right to file its complaints, that the defendants' own filings showed they had violated this Commission's rate of return prescription, and that this was enough to make out a *prima facie* case of a Communications Act violation sufficient to support a Section 208 complaint. The Bureau also stated that, although the record at that time arguably provided a legally adequate basis to support Commission action, it would provide the defendants an additional opportunity to show cause why this Commission should not order the payment of damages sought by MCI.

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[20] MCI v. PNB, DA 89-889 (released Jul. 27, 1989); MCI v. Pacific Bell, DA 89-890 (released Jul. 27, 1989); MCI v. SWB, DA 89-891 (released Jul. 27, 1989); MCI v. Wisconsin Bell, DA 89-892 (released Jul. 27, 1989); MCI v. C&P, DA 89-893 (released Jul. 27, 1989); MCI v. New Jersey Bell, DA 89-894 (released Jul. 27, 1989); MCI v. Mountain States, DA 89-895 (released Jul. 27, 1989); MCI v. Michigan Bell, DA 89-896 (released Jul. 27, 1989); MCI v. NWB, DA 89-897 (released Jul. 27, 1989); MCI v. Diamond States, DA 89-898 (released Jul. 27, 1989).

25. The Bureau's order also noted that the decision in *AT & T v. FCC* could be read to indicate that this Commission's automatic refund mechanism might have survived challenge if it had provided a means for taking into account the impact of a refund obligation on a carrier's overall rate of return. The Bureau stated that if a defendant elected to argue that this Commission should consider the impact on the defendant's overall return that would result from an award of damages, it should include in its response to the order to show cause a precise accounting of that impact. The Bureau also directed the defendants to provide a calculation of damages for each service and/or service segment as alleged in the complaints.[30]

26. The defendants filed responses to the show cause orders on August 16, 1989. MCI filed comments thereto on August 30, 1989. In addition, the three US West defendants filed a joint reply to MCI's comments, along with a contingent motion to accept the reply, on September 11, 1989.

27. The defendants' arguments in response to the show cause orders are based primarily on the contention that the statutory scheme of the Communications Act does not provide for the payment of reparations based upon profits earned under a lawfully filed and effective tariff; therefore, the defendants claim, MCI's complaints failed to state a *prima facie* case under Section 208 of the Act. Even if allegations that defendants earned in excess of the lawful return prescribed by the Commission could support a valid cause of action, the defendants claim that

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[30] In making the calculation, defendants were asked to assume a study area defined by the geographical reach of defendants' filed tariff, a maximum allowable rate of return of 13.1 percent per overall interstate earnings, and a maximum allowable rate of return for any access service category of 13.25 percent. Calculations were to be explained fully with evidentiary support adequate to allow the Bureau and complainant to evaluate defendants' arguments and support documentation.

such earnings would have to be measured on a "total company" basis, which some describe as the carrier that filed the tariff (*i.e.*, the Bell Operating Company level) and the US West carriers describe as the parent holding company level. In no event, the defendants contend, can this Commission lawfully enforce its rate of return prescription on a study area and access service category basis. Defendants argue that the Court in *AT & T v. FCC* found this type of rate of return enforcement mechanism to be unlawful. When considered in light of this decision, the defendants argue, MCI's complaints fail to state a claim upon which relief may be granted.

28. The defendants further claim that MCI's complaints are flawed in the same manner as the "automatic refund" mechanism struck down by the Court in *AT & T v. FCC*; that is, both the complaint and the automatic refund mechanism would have a carrier disgorge purported overearnings (*i.e.*, revenue "peaks") in individual access service categories without recognizing that such action will depress earnings below authorized levels because purported underearnings (*i.e.*, revenue "valleys") are not correspondingly uplifted to compensate. Several defendants claim that if MCI is awarded the damages it seeks, this Commission must find in the defendants' favor with regard to counter-claims they have filed against MCI to recoup earnings shortfalls.

29. Michigan Bell and Wisconsin Bell make the additional claim that the Bureau erred in ruling that the rates at issue were not Commission-prescribed but instead were carrier-initiated rates developed according to general Commission guidelines. Citing *Arizona Grocery v. Atchison, Topeka and Santa Fe Railway Co.*[21] and *Moss v. CAB*,[22] the defendants contend that the rates were the product of repeated Commission directives and cannot be said to reflect the free will of the carriers. According to the

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[21] 284 U.S. 370 (1932).

[22] 430 F.2d 891 (D.C. Cir. 1970).

defendants, the Commission not only set the formula and the maximum return, but also reviewed and rejected various nonconforming tariff filings with specific instructions on how the tariffs were to be revised. Thus, defendants contend, the subject rates were not carrier-initiated and the Bureau exceeded its lawful authority in holding that the rates are subject to retroactive reductions through an award of reparations or damages.

30. The defendants next contend that the Bureau's show cause orders are inappropriate in the context of Section 208 complaint proceedings and the Bureau's use of such an approach constituted procedural error. According to defendants, complaints for damages under Section 208 of the Act are adjudicatory proceedings, the resolution of which requires the complainant—not the defendant—to produce evidence of a violation and evidence of damages. The defendants maintain that due process and the Administrative Procedure Act [28] guarantee the defendants the right to challenge any evidence presented by the complainant and to submit evidence of their own. The defendants argue that the Bureau effectively short circuited these guarantees by shifting the burden of pleading and proving damages to the defendants. The defendants claim that the Bureau's approach is particularly inappropriate in light of the Court's ruling in *AT & T v. FCC* because that case, they argue, establishes that overearnings in individual access service categories do not necessarily translate into or reflect damages.

31. The defendant US West carriers make the additional claim that the Bureau "overstepped" its lawful delegated authority in issuing the show cause orders. According to US West, the Bureau may not lawfully adjudicate formal complaints, at least beyond dealing with facially defective complaints under the Commission's Rules. Otherwise, US West states, formal complaints must be designated for hearing under Section 0.291(e) of the

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[28] *See* 5 U.S.C. Section 552 *et seq.*

Commission's Rules. US West contends that the Bureau's show cause orders and the decisions rendered therein were unlawful and, therefore, should be vacated.

32. The defendants, with the exception of the US West Operating Companies, contend that, in any event, the damage computations required by the Bureau are inadequate to satisfy MCI's burden of proof because they do not and cannot show any damage to MCI. Defendants argue that the show cause orders are premised on the erroneous assumption that MCI would have paid in total a lesser amount for interstate access services if the defendants' rates in the overearnings categories had been less. Defendants maintain that this assumption is unsupported by the record and argue that MCI could have conceivably incurred the same or higher total costs if it had ordered and received either a greater volume of services or a different mix of services as a result of the hypothetical lower rates.[84] The defendants contend that without recalculating MCI's costs, rates, demand revenues and profits, it is impossible to conclude that MCI has been damaged by defendants' rates.

33. The defendants also restate the argument that MCI's claims for damages are partially barred by the two year statute of limitations contained in Section 415 of the Communications Act. The defendants contend that it is incorrect to conclude the two year limitations period did not begin to run until the defendants filed their rate of return monitoring reports on September 30, 1987 because MCI possessed sufficient information regarding the defendant's alleged overearnings which form the basis of its claims long before the monitoring reports were filed with the Commission. Therefore, defendants contend, the Bureau's failure to uphold the application of the statute of

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[84] Some of the defendants also argue that MCI has not been damaged by the rates in question because, even if the rates actually had been lower, MCI would have lowered its own rates in response to competitive pressure exerted by AT&T.

limitations to MCI's claims was incorrect as a matter of law and constitutes reversible error.

34. Finally, Pacific Bell contends that assuming the defendants are properly subject to damage claims, MCI should be denied prejudgment interest because MCI's request for interest is predicated on the Commission's grant of interest associated with amounts to be automatically refunded in the Docket 84-800 proceeding. Pacific Bell states that the court in *AT & T v. FCC* invalidated the automatic refund plan, including the obligation to pay interest on overearnings, and argues that therefore, MCI's request for prejudgment interest as provided in the Docket 84-800 proceeding may not be relied upon as a basis for an award of interest on any damages to which it may be entitled. Pacific Bell further contends that there is no statutory basis for such an award since neither Section 208 nor Section 209 of the Act, which together provide the basis for complaints under the Act and authorize the Commission to order the carrier to pay damages, provides for the payment of prejudgment interest.

35. In its reply to the defendants' responses to the Bureau order to show cause, MCI asserts that the Bureau's orders are valid. According to MCI, this Commission's rate of return prescription has binding, prospective effect; that rates earning in excess of the prescription are unlawful under the Communications Act; and that this Commission can order the payment of damages to a complainant in a proceeding in which, as here, a complainant establishes that a carrier's rates overearned and the complainant paid such rates. According to MCI, the payment of such damages does not constitute retroactive ratemaking but, instead, is merely the enforcement of a valid, prospective rate order. MCI also contends that defendants' overearnings on some rates are not excused by underearnings on other rates, and that there is no provision of the Act that will support the defendants' counterclaims against MCI to recoup past underearnings.

36. MCI contends that the holding in *AT & T v. FCC* is not as broad as the defendants contend and does not preclude the relief MCI seeks in its complaints. MCI states that the court in that case emphasized the Commission's authority to enforce its prescription authority by ordering refunds of carrier overearnings. MCI states further that although the court struck down the the [sic] portion of this Commission's prescription relating to the automatic refund mechanism, that mechanism plays no role in MCI's complaints and the remaining portions of the prescription have the same continuing legal effect as if *AT&T v. FCC* never had been decided. Moreover, MCI contends, a private complaint for damages cannot be equated with the automatic refund mechanism because: (1) a complaint is initiated by a customer instead of operating automatically in accordance with a Commission rule; and, (2) a complaint does not seek a refund of overearnings to a class of customers on a recurring basis but, instead, seeks the payment of damages to a particular complainant as reparations for injury suffered by that complainant during a specific, limited period.

37. Finally, MCI argues that the Bureau did not violate the defendants' due process rights by directing them to calculate the amount of damages. The order does not shift the burden of proving damages to the defendants, MCI claims, because the defendants already admitted the overearnings alleged by MCI; all that remains is for the defendants to ascertain the precise amount of damages based on information that is in their sole possession. According to MCI, the proper measure of such damages is the difference between the amount paid and the reasonable rate. MCI claims that there is no need for it to demonstrate the impact of their excessive rates on its profits in order to establish damages, and it further claims that the defendants' statements to the effect that AT&T was charged the same rates are irrelevant to these complaint proceedings. MCI also maintains that the Bureau acted well within its delegated authority in adopting and issuing the order.

IV. DISCUSSION

38. On the basis of our examination of the record, we conclude that complainant MCI has proven that the defendants violated the Communications Act and are liable to MCI to the extent it can establish that it was damaged thereby. MCI has chosen to pursue damages in a supplemental complaint, and it is entitled under our rules to proceed in this manner.[25]

39. The Communications Act grants private parties a right to file complaints against carriers and authorizes the FCC to award damages, 47 U.S.C. §§ 206, 208-209, and MCI filed its complaints against the defendants pursuant to these provisions. Under our rules, all that is required to make out a *prima facie* case in a complaint proceeding is a filing containing "facts which, if true, are sufficient to constitute a violation of the Act or Commission order or regulation . . . ." [26]

40. The case MCI presents is straightforward. The action it alleges the defendants have "done or omitted to be done" in contravention of the Act, 47 U.S.C. § 208, is to achieve earnings in excess of the Commission's order prescribing a rate of return applicable to the defendants, thereby making the rates MCI paid unjustly and unreasonably high in violation of Section 201(b) of the Act. In support of its allegations, MCI offered evidence in the form of monitoring reports filed with the Commission by the defendants which show that they earned returns in one or more categories in excess of the 13.25 percent allowable return provided for in the Commission's rules. MCI contends that it was damaged as a result of paying the defendants' rates.

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[25] Our rules provide that damages may be awarded in a supplemental complaint proceeding based on a determination by the Commission relating to the original complaint that it "contains appropriate allegations showing such evidence that will identify, with reasonable certainty, the amount of damages for which recovery is sought." 47 C.F.R. § 1.722 (1988).

[26] 47 C.F.R. § 1.720(b) (1988).

41. Defendants allege that MCI's complaints do not make out a *prima facie* case. The defendants do not dispute that the Commission prescribed a rate of return. Indeed, they affirmatively present selected aspects of that prescription as a defense to MCI's claims.[27] They admit that the reports they prepared and filed with the Commission show earnings in excess of 13.25 percent in one or more access categories. Thus, there are no disputed material facts in the record going to liability.[28]

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[27] As noted at para. 10, *supra*, in the prescription proceedings, the Commission established, *inter alia*, an authorized return for use in developing tariff rates and a "spread" or "buffer" above that return that would be used in proceedings relating to the enforcement of the prescription. During the period in question, LECs were notified that the maximum allowable rate of return for overall interstate earnings would be 13.10 percent, and that the maximum allowable return for any access service category would be 13.25 percent. The defendants rely on the continuing validity of the 13.10 percent overall interstate limitation as a defense to MCI's complaints. *See, e.g.*, US West Response to Order to Show Cause, at 20, Appendix A (alleging that US West Carriers' did not violate prescription because their aggregated overall interstate earnings was less than 13.10 percent).

[28] In their answers to MCI's complaints, Michigan and Wisconsin Bell assert that the methodology used to calculate the rates of return shown in their reports overstates their actual returns, but they neither discuss nor explain this contention. The methodology was developed and adopted in a Rule Making proceeding in which the Commission established a uniform method of calculating carriers' interstate rates of return for use in the enforcement of our rate of return prescriptions and to assist us in the tariff review process. *See Amendment of Part 65, Procedures and Methodologies to Establish Reporting Requirements, Report and Order*, CC Docket No. 86-127, FCC 86-514 (released Dec. 3, 1986), 51 Fed. Reg. 273 (Jan. 5, 1987). The monitoring reports are entitled "FCC Form 492, Rate of Return Report" and carriers are required to file them with the Commission on a quarterly basis. *See* 47 C.F.R. § 65.600(b). The defendants participated in that Rule Making. They neither sought reconsideration nor pursued an appeal of decisions concerning the methodology. Therefore, their assertions about that methodology do

42. The defendants argue that judgment cannot be entered for MCI for reasons that fall into four general categories. The first contains arguments that earning in excess of a rate of return prescription is not a violation of the Act or any valid Commission rule or order; and, even if such action could be considered a violation, it could occur only if the return was exceeded by the company "overall." Included in this first category is the argument of several defendants that a carrier cannot violate the Act by charging the rates in its tariff. In the second category are arguments that MCI cannot recover because the rates in effect during the period in question were prescribed by the Commission, not carrier-initiated. Category three contains claims that MCI's complaints are barred by the statute of limitations. In the fourth category are arguments that the defendants' due process rights have been violated by the Common Carrier Bureau's orders to show cause. We discuss each category, in turn, below.

A. *Violation of the Act*

43. This category contains several different arguments by the defendants as to why MCI's complaints are invalid. Several defendants claim that an award of the damages it seeks would constitute retroactive ratemaking.[39] Wisconsin Bell contends that MCI's action is barred because it seeks, "in effect," a remission of tariffed charges in contravention of Section 203(c) of the Act.[40] US West states that the "notion that a carrier could violate the Communications Act by charging the amounts specified in its tariffs would appear ludicrous on its face."[41]

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not create a dispute about a material fact but are, instead, impermissible collateral attacks on decisions adopted in a proceeding in which their right to review has expired.

[39] *See, e.g.*, US West Carriers Response to Order to Show Cause, at 13-15; Bell Atlantic Response to Order to Show Cause, at 5.

[40] Wisconsin Bell Motion to Dismiss, at 15 n.29.

[41] US West Response to Order to Show Cause, at 14.

44. The broadest argument in this category is made by US West, which claims that earnings in excess of this Commission's prescribed return cannot establish a violation of the Act because "the statute *never* mentions 'excessive returns'—it requires a complainant to demonstrate a violation of the Act and the Act only speaks of *'rates,'* not 'returns.' "[42] In support of its additional claim that high profits do not necessarily establish that a rate is unjust and unreasonable, US West quotes a number of different authorities. These include a statement from the court's opinion in *Nader v. FCC* that "a rate of return is just one component of a rate,"[43] as well as the Commission's statement in its order adopting the prescription: " 'returns that slightly exceed . . . a target [return] have never been and should not be deemed unjust.' "[44]

45. All of the defendants claim that MCI's complaints are barred as a result of the holding in *AT & T v. FCC*, which invalidated the Commission's procedure to enforce its rate of return prescriptions through automatic refunds of carrier overearnings to categories of customers.[45] This

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[42] *Id.*, at 26 (emphasis in original).

[43] US West Motion to Dismiss, at 2, quoting *Nader v. FCC*, 520 F.2d 182, 201 (D.C. Cir. 1975).

[44] US West Motion to Dismiss, at 10 citing *Phase I Order*, at para. 36. US West also quoted *The Western Union Telegraph Company*, 95 FCC 2d 881, 910 (1983) ("We believe that Telex usage element earnings which exceed the prescribed earnings level for Telex service overall by only 1 or 2 percentage points do not render the service element rates unreasonable[.]"). US West also claimed that the holding in *AT & T v. FCC* implies that rates earning in excess of a rate of return prescription are not unjust or unreasonable. *Id.*

[45] US West Reponse to Order to Show Cause, at 4, 10-17; Pacific Bell Response to Order to Show Cause, at 5-7; SW Bell Reponse to Order to Show Cause, at 6; Wisconsin Bell Reponse to Order to Show Cause, at 16-18; Michigan Bell Response to Order to Show Cause, at 16-18; C&P Response to Order to Show Cause, at 3-6; New Jersey Bell Response to Order to Show Cause, at 3-6; Diamond State Response to Order to Show Cause, at 3-6.

claim is presented in two arguments. Pacific states the first most succinctly:

> The Commission's refund rule required carriers to automatically refund earnings in excess of the authorized rate of return. For refund purposes, the Commission viewed the rate of return as a maximum return. However, the Commission has always treated the rate of return for ratemaking purposes as the minimum and maximum return. In *AT & T*, the court found that these differing concepts resulted in the Commission's contradicting its own theory of rate of return regulation. Because of this contradiction, the court found the Commission's action to be arbitrary and capricious and invalidated the refund rule . . . . Merely changing the remedy from a "refund" to a "damage award" does not cure this fundamental infirmity.[46]

46. The gist of the defendants' second argument is that under the holding in *AT & T v. FCC*, the Commission must consider a carrier's underearnings in determining whether particular overearnings are in violation of the Act. This "peaks and valleys" argument is presented several different ways. Pacific suggests that the case bars all damage awards because even a system permitting damages for "overall overearnings" in any particular period would virtually guarantee an earnings shortfall for all such periods viewed together.[47] Other defendants admit that a judgment could be made about earnings in a particular period, but advance different methods of calculating "overall" earnings within the period. For example, US West contends that overearnings could be judged only according

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[46] Pacific Response to Order to Show Cause, at 6-7. *See also* US West Response to Order to Show Cause, at 14.

[47] *Id.*, at 8. Pacific also provides evidence that it earned 13.09 percent on its interstate operations during the period covered by MCI's complaint. Pacific argues that this return is "below the maximum authorized rate of 13.1 percent" and, "[t]herefore, no refund or damage award is due MCI." *Id.*, at 9.

to the aggregated returns of all its operating companies because " 'investors in a carrier, after all, must invest in the carrier as a whole.' " [48] In a consolidated pleading, defendants C&P, New Jersey Bell, and Diamond State, seek to have their earnings measured at their individual corporate levels, rather than in relation to each other or to other subsidiaries of their parent holding company, Bell Atlantic.[49]

47. After careful consideration of the pleadings, we conclude that the defendants' arguments have no merit.

48. Wisconsin Bell offers no support for its claim that MCI's complaints are barred by Section 203 of the Act, nor did US West support its contention that a carrier cannot be found to have violated the Act by charging the rates in its tariff. Contrary to the defendants' claims, however, legally effective, carrier-initiated tariffs can always be challenged as unreasonable and unlawful. As the Supreme Court has stated:

> In order to render rates definite and certain, and to prevent discrimination and other abuses, the statute required the filing and publishing of tariffs specifying the rates adopted by the carrier, and made these the *legal* rates, that is, those which must be charged to all shippers alike.
>
> Although the Act thus created a legal rate, it did not abrogate, but expressly affirmed, the common-law duty to charge no more than a reasonable rate, and left upon the carrier the burden of conforming its charges to that standard. In other words, the legal rate was not made by the statute a lawful rate—it was lawful only if it was reasonable . . . . [The]

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[48] US West Response to Order to Show Cause, at 19, citing *AT & T v. FCC*, 836 F.2d at 1392.

[49] *See* Bell Atlantic Answer and Motion to Dismiss, at 2. These defendants claim they have not overearned because each of them earned less than 13.1 percent for the period in question.

shipper was bound to pay the legal rate; but if he could show that it was unreasonable he might recover reparation.[50]

49. Moreover, the defendants, in claiming that high profits do not necessarily mean a rate is unreasonable, miss the point. The issue in these proceedings is not whether high profits in the abstract are unlawful, but whether profits in excess of a prescription are unlawful. US West invokes and relies upon this Commission's statement that "returns that slightly exceed a target [return . . . have never been and should not be deemed unjust." That statement is not helpful to US West, however, because it is part of the explanation of our rationale for establishing, above the targeting return, a buffer that would be used to determine whether a prescribed return had been violated. MCI has taken that buffer into account in filing its complaints. In context, the statement stands for the proposition that carrier earnings over and above the buffer—like those US West has admitted to during the period covered by MCI's complaints—are unlawful.

50. The defendants' arguments would be persuasive only if one assumed that a rate of return prescription requires carriers to target their rates at that level but has no meaning in relation to the actual performance of those rates. This assumption conflicts with settled law.

51. The Commission has authority under the Communications Act to prescribe carriers' rates of return.[51]

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[50] *Arizona Grocery v. Atchison, T. & S. F. R. Co.*, 284 U.S. 370, 384 (1932) (emphasis in original) (footnotes omitted). In this case, the Court was interpreting sections of the Interstate Commerce Act (ICA) establishing private actions for damages. These sections were lifted from the ICA by Congress when it adopted the Communications Act in 1934 and have remained essentially unchanged since that time. *Compare* 49 U.S.C. §§ 6-9 *with* 47 U.S.C. §§ 206-209. For that reason, the Commission often looks to cases decided under the ICA for guidance in deciding complaint cases.

[51] *Nader v. FCC*, 520 F.2d 182 (D.C. Cir. 1975).

In upholding this authority, the D.C. Circuit determined that rate of return prescriptions are a valid exercise of our authority under Sections 4(i) and 205 of the Act, and that such prescriptions are "necessary for the Commission to carry out its [ratemaking] functions in an expeditious manner." [52]

52. The prescription of a rate of return establishes a requirement more far-reaching than merely that it be used in the development of a carrier's rates.[53] As the court in *Nader* explained, a rate of return prescription, like any other Section 205 prescription, is binding: it limits the utility prospectively.[54] Subsequent to the *Nader* decision, the binding effect of such a prescription was reaffirmed by the D.C. Circuit in *New England Telephone.* In its opinion in that case, the court emphasized that an order setting a maximum rate of return is "a valid Section 205 prescription" having the "force of statute . . . . The carrier . . . is bound to conform".[55] In addressing the targetting argument directly, the court stated:

> Petitioners . . . contend that the nature of their obligation was merely to try in good faith to formulate rates that would not produce an excessive return. In the Commission's view, by contrast, the prescription imposed a maximum return that the carriers could not exceed, however innocently . . . .
>
> The idea of a prescription under Section 205 is that the agency has proclaimed that a certain situation

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[52] *Id.*, 520 F.2d at 204.

[53] Carriers are bound to abide by validly promulgated Commission orders until they are superseded. 47 U.S.C. § 408 (1982). More particularly, carriers must adhere to prescription orders until the Commission approves a different course of conduct. 47 U.S.C. § 205(a) (1982).

[54] *Nader v. FCC*, 520 F.2d at 203-204.

[55] *New England Telephone*, 836 F.2d at 1106, 1107, quoting *Arizona Grocery v. Atchison Ry.*, 284 U.S. 370, 386 (1931).

> . . . is unlawful and *shall not occur*. Certainly carriers cannot intentionally try to violate an outstanding prescription, but that does not mean that they may achieve through inadvertance what they were forbidden from doing by design.[56]

53. Contrary to the defendants' assertions, the case law supports MCI's argument that the enforcement of a rate of return prescription does not violate the rule against retroactive ratemaking, for a simple reason: the obligation being enforced was set prospectively when the prescription was adopted. The defendants either do not address the *New England Telephone* case, which MCI presents as support for its complaints, or dismiss the case as a departure from precedent.[57] But none of the decisions cited by the defendants supports a contrary view. With one exception, none of those decisions involved an existing, prospectively defined prescription. The exception, *AT & T v. FCC*, also provides no support for their claims about retroactive ratemaking or the limited reach of rate of return prescriptions. The court in *AT & T v. FCC* explicitly acknowledged the Commission's authority to order a carrier to disgorge earnings in excess of a rate of return prescription.[58]

54. We are also not persuaded by the defendants' other claims that the holding in *AT & T v. FCC* controls these proceedings and bars judgment for MCI. In that case, the court determined that the remedy component of the Commission's rate of return prescription—the automatic refund

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[56] *New England Telephone*, 826 F.2d at 1106 (emphasis in original).

[57] *See, e.g.*, US West Response to Order to Show Cause, at 18-19 n.51.

[58] *AT & T v. FCC*, 836 F.2d at 1392 ("Thus, as we previously have concluded, the Commission has authority under the Act to order refunds where a carrier has violated an outstanding rate-of-return prescription").

mechanism—was unlawful. The defendants argue that in striking down a remedy conceived by the Commission and based on its authority under Sections 4(i) and 205, the D.C. Circuit also invalidated private actions for damages conceived by Congress and expressly provided for in Sections 206 through 209 of the Act. This argument finds no support in the court's opinion.

55. The opinion of the court distinguishes the automatic refund mechanism from the prescription as a whole, finding only the former invalid.[59] That mechanism plays no role in these complaint proceedings. Moreover, the automatic refund mechanism and private actions for damages are distinctly different from each other. The automatic refund mechanism resulted from a Rule Making initiated at the Commission's discretion. In contrast, private actions for damages were established by the Congress as part of the Act. They do not operate automatically, nor are complainants members of a class of customers defined by the Commission. Complainants do not seek the benefit of a future rate reduction, as the automatic refund mechanism provided. Each complaint must be initiated by a private party seeking damages for an injury *to itself*, and that party carries the burden of establishing both a violation of the Act and the actual injury.[60] If a complainant

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[59] *Id.*, 836 F.2d at 1392.

[60] The complaint provisions of the Act make a carrier liable to its customers for damages that result from the carrier's unlawful actions or ommissions. 47 U.S.C. §§ 206-209 (1982). These sections of the Act do not provide a basis for a carrier to file a complaint against its customers. *See Illinois Bell Telephone Company, et al. v. American Telephone and Telegraph Co.*, 4 FCC Rcd. 5268 (1989). In the instant proceeding, US West filed cross-complaints against MCI to recover underearnings. Although MCI is a carrier, the pertinent inquiry for determining the applicability of complaint procedures focuses on the relationship between the complainant and defendant with regard to the action in question. Here, US West is alleging it has been damaged by providing service as a carrier to a customer, MCI. There is no basis for such a complaints under the Act and, therefore, US West's cross-complaints are dismissed.

meets this burden, the Act expressly authorizes the Commission to order the carrier to pay damages.[61]

56. Moreover, the defendants do not offer a plausible basis for reading the opinion in *AT & T v. FCC* as they suggest. The opinion does not address Section 208 complaint proceedings nor purport to alter the statutory scheme of the Act or the remedies Congress established therein. Although the defendants invoke the decision in support of a broad constitutional claim that the Commission must take their underearnings into account when considering private actions for damages resulting from earnings in excess of a prescription, the court explicitly declined to base its decision on constitutional grounds.[62] The court's discussion of constitutional issues appears in a portion of the opinion separate from the holding, and consists of "guidance" offered "in case the Commission chooses to reformulate the refund rule." [63]

57. In any case, the Constitution does not prohibit the Commission from ordering damages when a carrier has overearned in a service category. The implication of the defendants' claim is that they are entitled, as a constitutional matter, to charge their customers excessive rates for one category of service as long as these earnings are balanced by a deficiency in earnings in another category; in short, that they are entitled to cross-subsidize. This clearly is not the case. The prevention of cross-

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[61] 47 U.S.C. § 209 (1982).

[62] After noting that the plaintiffs in *AT & T v. FCC* asserted that the refund rule violated the Communications Act, the Constitution, and the Administrative Procedure Act's prohibition of arbitrary and capricious agency action, the court stated: "We find one of these challenges dispositive. We agree that the Commission's refund rule is arbitrary and capricious agency action under the Administrative Procedure Act." *AT & T v. FCC*, 836 F.2d at 1389 (citations deleted).

[63] *Id.*, at 1391-93.

subsidization has long been recognized as a lawful objective of rate regulation.[64] Regulatory agencies have the authority, indeed the duty, to protect ratepayers from such exploitation.[65]

58. Courts have made clear that carriers assume the risk of both losses for services they underprice and the prospect of returning amounts realized through rates that are unjustly and unreasonably high.[66] The case law also indicates that a carrier may be required to make whole those who have been injured by discrimination and cross-subsidized rate structures without regard to whether the carrier has achieved its authorized return overall.[67]

59. It does not disturb the balance of ratepayer and shareholder interests embodied in the Act to award damages to customers who demonstrate that they were injured by paying rates that resulted in a carrier earning in excess

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[64] *See Nader v. FCC*, 520 F.2d at 201.

[65] *Jersey Central Power & Light Co. v. FERC*, 810 F.2d 1168, 1180-81 (D.C. Cir. 1987).

[66] *See, e.g., FPC v. Tennessee Gas Pipeline Co.*, 371 U.S. 145, 153 (1962) ("a rate for one class or zone of customers may be found by the Commission to be too low, but the company cannot recoup its losses by making retroactive the nigher rate subsequently allowed; on the other hand, when another class or zone of customers is found to be subject to excessive rates and a lower rate is ordered, the company must make refunds to them. The company's losses in the first instance do not justify its illegal gain in the latter."); *TRT Communications v. FCC*, 837 F.2d 1535, 1553 (D.C. Cir. 1988) ("[T]hat a carrier is made subject to refunds or reparation claims, accompanied by a liability for interest, is part of the price it pays for the flexibility in a scheme of carrier-initiated rates. The carrier retains the flexibility to effect a rate increase, but it must account for its increased revenues if those rates are later found to be unlawful."); *see also Communications Satellite Corp. v. FCC*, 611 F.2d 883, 892-94 (D.C. Cir. 1977).

[67] *See Nader v. FCC*, 520 F.2d at 201, 202-203; *MCI Communications Corp. v. FCC*, 675 F.2d 408, 410 (D.C. Cir. 1982).

of its prescribed return. Even when a carrier operates under a prescription of a rate of return for broad categories, the carrier retains substantial flexibility in formulating rates.[68] Carriers are permitted to make mid-course corrections if their actual return deviates from the authorized return. If actual earnings are higher than the authorized return, a carrier can file reductions and thereby avoid the risk of being ordered to pay damages. If actual earnings are below the authorized return, a carrier can file rate increases. Defendants had ample notice of our rules, which were developed in notice and comment Rule Making proceedings in which all of them participated, as well as the level of the prescription for each category. As a general matter, it would be inequitable to permit defendants, who were in the best position to set their rates at lawful levels in the first place, and who later had opportunities to correct those rates, to avoid responsibility for those unlawful rates, at the expense of their customers.

60. Against this background, we are not persuaded by the defendants' claims that earning in excess of a prescribed rate of return does not violate the Act or, if it does, that the Commission *is required* to take a carrier's underearnings as well as its overearnings into account in determining whether a violation has occurred.[69] The first claim is at odds with case law, including *Nader, New*

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[68] *See Nader v. FCC*, 520 F.2d at 201.

[69] As described in paragraphs 10-13, *supra*, the Commission in its Rule Making proceeding built safeguards into its prescription to ensure that carriers would have reasonable opportunity to achieve their authorized return while having their rates reviewed at the category level. All of these safeguards provided carriers with substantial flexibility to offset peak and valley earnings, in a manner consistent with the Commission's statutory obligation to prevent discrimination among users of access services. The Commission's decision to provide this flexibility, and the particular manner in which it was provided, are not at issue in the instant complaint proceedings.

England Telephone, and *AT & T v. FCC*.[70] Contrary to the defendants' contentions, the holding in *AT & T v. FCC* provides no support for their second claim. Indeed, as discussed previously, the rationale underlying this claim has been rejected explicitly by the D.C. Circuit and the Supreme Court.[71] We find that a valid prescription bound the defendants to a maximum earnings limitation, and the defendants admit that they earned in excess of that amount during the period in question.

61. Finally, with regard to the defendants' second claim, and MCI's claim to the contrary, that we lack discretion in proceedings under Sections 206-209 of the Act to consider a defendant's "peak" and "valley" earnings,[72] the Common Carrier Bureau's orders to show cause stated:

> If in response to this order to show cause, however, defendant elects to argue that the Commission *should* consider the impact on the defendant's overall return that would result from an award of damages in the instant proceeding, the defendant should include in its response a precise accounting of that impact.[73]

62. Pacific's submission in response to that show cause order indicates that its "total company" earnings would exceed prescribed levels even after an award of damages to MCI. The C&P Companies' submission shows that an award of damages would have a *de minimis* impact on its "total company" earnings, lowering them from 12.38 percent to 12.37 percent. Similar *de minimis* impacts are reflected in the submissions of New Jersey Bell (from

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[70] *See also Communications Satellite Corporation*, Memorandum Opinion and Order, 3 FCC Rcd 2643 (1988), *aff'd mem., Communications Satellite Corporation v. FCC*, No. 88-1243 (D.C. Cir. Nov. 17, 1989).

[71] See paras. 57-59, *supra*, and notes therein.

[72] MCI Reply at 24 & n.73.

[73] *See, e.g.*, MCI v. Pacific Bell, Order to Show Cause, 4 FCC Rcd 6116, 6117 at n.7 (1987) (emphasis added).

13.03 percent to 12.98 percent) and Diamond State (from 12.36 percent to 12.34 percent). The remaining defendants declined to provide an accounting of the impact on their earnings of a potential damage award to MCI.[74] This record provides no basis for resolving questions concerning this Commission's discretion to consider the relevance of "peak and valley" earnings in a rate of return complaint proceeding, and we will not do so in the course of resolving the instant complaints.

B. *Rates In Effect Were Prescribed By Commission*

63. Michigan Bell and Wisconsin Bell contend that MCI's complaints are barred because the rates in effect during the period in question were prescribed by the Commission. The defendants' arguments are not persuasive.

64. It is well-settled law that the prescription of a rate of return is not a prescription of rates. In *Nader v. FCC*, 520 F.2d 182, 201 (D.C. Cir. 1975), the court stated: "[W]e cannot agree that the Commission has literally prescribed rates, for the charge itself cannot be equated with a rate of return . . . . a rate of return is merely one component of a rate." Thus, in prescribing the rate of return component of the defendants' rates, the Commission did not prescribe the rates themselves.

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[74] Instead of submitting calculations of the impact on overall earnings of potential damage awards to MCI, US West submitted calculations showing the impact on overall earnings "after capping category returns at 13.25%." US West Response at Appendix B. In other words, US West's submission shows the impact on its earnings that might have resulted if one assumed that all interexchange carriers that took service from US West had filed complaints relating to the period in question. The results filed by US West cannot occur, however, because all such carriers did not file complaints against US West.

For the record, however, the US West submission shows that on a state-by-state basis, which was the geographic level at which its operating companies chose to file tariffs during the period in question, earnings would be affected as follows: Arizona (from 12.26% to 11.91%), Colorado (no change), Idaho-

65. Nor can it be argued plausibly that the defendants' rates were prescribed merely because the defendants were required to conform such rates to the Commission's Part 69 access charge rules. While Part 69 of our rules defines major aspects of the defendants' interstate rate structure, and includes many steps they must follow in order to compute rates, the D.C. Circuit already has held that such rules do not "determine the legality of specific rates." [75]

66. The defendants, however, also argue that the rates complained of by MCI were the product of their response to Commission orders relating to its review of their access tariff filings during the period from October 3, 1983 to April 1, 1985. These orders, defendants allege, were so detailed as to leave to them merely the performance of "the ministerial task of gathering data, plugging the data into the Commission's formula, and doing mathematical computations to arrive at the access tariff rates"; and, therefore, the resulting rates were not carrier-initiated but, instead, were the result of a rate prescription.[76]

67. The question whether an agency prescribed a rate must be determined by looking at the practical consequences of its actions.[77] As the court in *Direct Marketing Association, Inc. v. FCC*, 772 F.2d 966, (D.C. Cir. 1985), after surveying the case law, concluded:

MNT (from 12.85% to 12.17%), Montana (from 12.82% to 12.20%), New Mexico (from 13.16% to 12.56%), Utah (from 12.51% to 12.36%), Wyoming (from 12.63% to 12.23%), Iowa (from 13.61% to 12.90%), Minnesota (from 13.29% to 12.83%), Nebraska (from 13.71% to 12.74%), North Dakota (from 15.19% to 12.81%), South Dakota (no change), Idaho-PNB (from 12.04% to 11.88%), Oregon (from 12.80% to 12.28%), Washington (no change).

[75] *National Assoc. of Reg. Commr's v. FCC*, 737 F.2d 1095, 1120 (D.C. Cir. 1984), *cert. denied*, 105 S.Ct. 1224 (1985).

[76] Wisconsin Bell Response to Order to Show Cause, at 9-16.

[77] *See Nader v. FCC*, 520 F.2d at 199.

> [T]he courts have considered the amount of pressure on the subject of the order, as measured by the options available to the subject and the amount of threat that the agency will suspend nonconforming tariffs. In practice, an agency statement has not been found to be a prescription absent explicit language that nonconforming tariffs will be rejected, combined with an agency motive to avoid public scrutiny and perhaps even judicial review.[78]

68. Thus, the test for determining whether a *de facto* prescription exists has two parts: (1) the degree of pressure imposed by the Commission and its impact on a carrier; and (2) the possibility that the Commission did not state it was acting under Section 205 of the Communications Act, 47 U.S.C. § 205, in order to avoid the public hearing required by that section. The defendants have not persuaded us that either part of this test has been satisfied with regard to the rates at issue in these complaint proceedings.

69. The Commission orders cited by the defendants were adopted during our review of the initial attempts by local exchange carriers (LECs) to tariff interstate services in accordance with our access charge plan.[79] The tariffs implementing that plan revised the rates and terms for nearly every interstate telecommunications service. Although, as noted previously, that plan establishes an overall rate structure for LECs and a methodology for allocating many costs within that structure, the plan does not determine the carriers' costs or the forecasts on which their proposed rates are based.

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[78] *Direct Marketing*, 772 F.2d at 971.

[79] In orders adopted during the year prior to these filings, this Commission established a single, uniform mechanism through which local exchange carriers would recover the cost of providing services needed to originate and terminate interstate and foreign telephone calls. *See MTS and WATS Market Structure*, 93 FCC 2d 241 (*Access Charge Order*), *on reconsideration*, 97 FCC 2d 682 (1983).

70. In carrying out our responsibility to review these filings, the Commission found, *inter alia*, that the carriers' representations about their costs and forecasts raised substantial concerns about the lawfulness of their rates. Therefore, pursuant to the Act, we initiated a comprehensive investigation of the tariffs "to resolve at least the major issues necessary to assure that generally reasonable, workable access tariffs are in place . . . ." [80] In that investigation, we adopted a series of orders either rejecting LEC filings or suspending them for purposes of investigation.

71. The defendants do not offer evidence that these proceedings were conducted in a manner designed to avoid the public hearing requirement of Section 205 or judicial review. A review of the record of these proceedings demonstrates the contrary. The Commission's rules provide for public participation in tariff proceedings.[81] Interested parties availed themselves of the opportunity to participate in these proceedings and their comments were considered by the Commission.[82] Thus, this aspect of the test for determining a *de facto* prescription is not satisfied.

72. The defendants assert, correctly, that the orders all contained an explanation of the basis for our actions and provided guidance, including specific instructions about actions that needed to be taken to bring access tariffs into compliance with the Act. The defendants argue that the orders must constitute a rate prescription because they

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[80] *Investigation of Access and Divestiture Related Tariffs*, 97 FCC 2d 1082, 1085 (1984) (*Order Initiating Investigation*).

[81] Our rules explicitly provide an opportunity for public participation in tariff proceedings, and establish specific methods for that participation. *See* 47 C.F.R. § 1.773 (1988).

[82] *See, e.g., Order Initiating Investigation*, 97 FCC 2d at 1083-1084, Appendix A (decisions adopted by Commission based on examination of tariffs, support materials, and comments filed by 55 interested parties).

were required to comply. They offer no specific examples of particular instructions, but appear to be arguing that the act of providing guidance and establishing requirements, in and of itself, demonstrates that rates filed in response to our orders were prescribed.[83] This is not the law.

73. The Act provides for Commission review of carrier rates.[84] Such review would be meaningless if it could not result in constraining the carriers' actions, and it would be considerably more time-consuming if the Commission were not permitted to give carriers some guidance as to what might be acceptable. In addressing this issue on review of actions similar to those at issue here, the Supreme Court stated:

> No principle of law requires the Commission to engage in a pointless charade in which carriers . . . are required to submit and resubmit tariffs until one finally below an undisclosed maximum point of reasonableness is allowed to take effect. The administrative process after all, is not modeled on "The Price is Right." [85]

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[83] The defendants cite *Moss v. CAB*, 430 F.2d 891 (D.C. Cir. 1970), as dispositive, but this is unpersuasive. In that case, the Civil Aeronautic Board, after private meetings with airline representatives, announced that it would accept only tariffs implementing "a detailed formula for determining fares." *Id.*, 430 F.2d at 895. By contrast, this Commission's proceedings were marked by active public participation, and did not result in the adoption of a detailed rate-calculation formula.

[84] 47 U.S.C. §§ 203-204 (1982).

[85] *Trans Alaska Pipeline Rate Cases*, 436 U.S. 631, 653 (1978). In the case, the Court considered whether the Interstate Commerce Commission (ICC) had prescribed rates for the transportation of North Slope oil. The ICC had suspended the initial tariffs filed by the pipeline owners and calculated "new rates that approximated what full investigation would likely reveal to be lawful rates." 436 U.S. at 637. The ICC stated that it would not suspend interim tariffs which "specified rates no higher than those estimated." *Id.* The Court held that this action did not amount to a prescription of rates.

74. The defendants also offer quotes from various orders which contain the word "prescription." These quotes do not, however, refer to the prescription of rates. The fact that the Commission may have prescribed certain aspects of the rate structure does not mean the rates themselves were prescribed. Moreover, if it were true that the rates filed in response to the orders actually were prescribed, the carriers would not have been free to change those rates until further order by this Commission. In fact, the entire LEC industry, including the defendants, revised their access tariffs comprehensively *after* the orders cited by the defendants were adopted. These revisions occurred *before* the October 1985 through December 1986 period covered by MCI's complaints.[86] Thus, the defendants have not demonstrated that the second component of a *de facto* prescription existed with regard to these rates.

75. Against this background, we find that the defendants have not established that the rates they charged during the period at issue in these proceedings were prescribed.

C. *Statute of Limitations*

76. The defendants make two claims with regard to the statute of limitations. The first, raised by US West, is that it is immaterial when a complainant learns of the fact that a carrier has exceeded a prescribed rate of re-

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[86] Pursuant to our rules, the LECs filed access tariff revisions in July 1985, four months after the last order referenced by the defendants. In an order allowing these revisions to take effect, the Common Carrier Bureau specifically referenced the existence of the Part 65 automatic refund mechanism as one reason for not preventing the tariffs from becoming effective. *Annual 1985 Access Tariff Filings,* Mimeo No. 7401, paras. 56-57, released Sept. 30, 1985. Even during the investigation, this Commission indicated that the LECs could file tariff revisions, if they so desired. *See Investigation of Access and Divestiture Related Tariffs,* 102 FCC 2d 1007, 1035-1037 (1985).

turn because such earnings are not sufficient to establish a *prima facie* case of unlawfulness under the Communication Act.[87] This claim cannot stand in view of our previous determination that violating a rate of return prescription does, indeed, constitute a violation of the Act.

77. The defendants' second claim is that all or a portion of MCI's claims are barred by Section 415 of the Act, which establishes a two year statute of limitations on the filing of complaints.[88] According to the defendants, Section 415 bars MCI's complaints at least for rates paid prior to February 9, 1986, two years before the date on which it filed its complaints.

78. This argument is not persuasive. The purpose of Section 415 is to protect a potential defendant against stale and vexatious claims by ending the possibility of litigation after a reasonable period of time has elapsed.[89] The statute does not begin to run, however, until discovery of the right or wrong or of the facts on which such knowledge is chargeable in law.[90] Here, the defendants filed the rate of return monitoring reports which, as previously noted, were developed by the Commission for

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[87] *See, e.g.*, US West Response to Order to Show Cause, at 25-26.

[88] Section 415 provides, in pertinent part, that "all complaints against carriers for the recovery of damages not based on overcharges shall be filed with the Commission within two years from the time the cause of action accrues, and not after . . . ." 47 U.S.C. § 415(b) (1982). The term "overcharges" is defined in Section 415 to mean "charges for services in excess of those applicable thereto under the schedules of charges lawfully on file with the Commission." 47 U.S.C. § 415(g) (1982).

[89] *Bunker Ramo Corp.*, 31 FCC 2d 449, 453 (1971).

[90] *Id.*, 31 FCC 2d at 454. Thus, *Atchison, T. & S.F.R. Co. v. ICC*, 851 F.2d 1432 (D.C. Cir. 1988), cited by the defendants, is inapposite. In that case, the claimants had sufficient notice of a potential refund claim, but were uncertain of the viability of the claim in view of ongoing lititation. 851 F.2d at 1439.

several purposes, including making information about carrier earnings publically available. Moreover, the monitoring reports relied on by MCI in its complaints were specifically designated by the Commission as a "final" and conclusively binding determination of a carrier's earnings.[91] Under these circumstances, Section 415 poses no bar to MCI's complaints.

D. *The Bureau's Show Cause Orders*

79. The arguments in support of defendants' claim that the Common Carrier Bureau overstepped its delegated authority are advanced primarily by the US West defendants, although all of the defendants generally argue that the Bureau exceeded its authority in adopting the show cause orders. These claims rest on the assumption that the Bureau has no authority to act in complaint proceedings. This assumption is incorrect.

80. The general authority of the Bureau with respect to the adjudication of Section 208 complaints is firmly established in Sections 0.91 and 0.291 of the Commission's Rules.[92] Section 0.291 expressly delegates to the Chief of the Common Carrier Bureau the "authority to perform all functions of the Bureau, described in Section 0.91" unless otherwise specifically limited. Section 0.91 (a) empowers the Bureau to act "for the Commission under delegated authority, in matters pertaining to the

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[91] 47 C.F.R. § 65.600(b) (1987); *see also Amendments of Part 65, Procedures and Methodologies to Establish Reporting Requirements*, CC Docket No. 86-127. Notice of Proposed Rule Making, 51 Fed. Reg. 15020, 15021 at para. 21 (Apr. 22, 1986); *Id.*, Report and Order, 52 Fed. Reg. 273 (Jan. 5, 1987). Carrier reports filed prior to the close of the review period could not be determinative of a carrier's earnings for the period as a whole. The Commission concluded that the quarterly filing on September 30th following the end of the period would provide a carrier sufficient opportunity to make appropriate accounting adjustments and "close its books," so to speak, with regard to the period.

[92] 47 C.F.R. §§ 0.91 and 0.291 (1988).

regulation and licensing of communications common carriers," which encompass "*adjudicatory* and Rule Making proceedings, including *rate* and service investigations [and] determinations regarding *lawfulness of carrier tariffs.*" (Emphasis added.) Because Section 0.91 plainly includes the authority to act for the Commission in connection with a Section 208 complaint, there can be no question under these rules of the Bureau's authority to issue the show cause orders.[93]

81. The Bureau's delegated authority under Part 0 of our Rules must, of course, be consistent with the Communications Act. The Bureau's delegated authority to act in complaint proceedings has been affected by 1988 amendments to Section 5(c)(1) of the Communications Act, but not in any way related to the action complained of by the defendants. These amendments reserve to the Commission the authority to adjudicate certain Section 208 complaints.[94] The show cause orders, however, do not purport to be a determination of unlawfulness or liability as to any aspect of MCI's complaints; rather, orders to show cause are, by their very nature, interlocutory. They are nothing other than a lawful attempt by the Bureau to facilitate the Commission's ability to issue a decision on the merits in these complaint proceedings within the statutory timeframe.[95]

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[93] Contrary to US West's suggestion, Section 0.291(e) does not require that formal complaints be designated for a hearing. Rather, it simply states that if certain formal complaints are to be designated for hearing, such designation must be made by this Commission.

[94] Pub. L. No. 100-594, 102 Stat. 3021 (1988) (to be codified at 47 U.S.C. § 151(c)(1)). *See also* 100 CONG. REC. S.15289 (daily ed. Oct. 7, 1988) (remarks of Senator Inouye) (order concluding investigation initiated by certain complaints "shall be issued by the Commission").

[95] *See* Pub. L. No. 100-594, 102 Stat. 3021 (1988) (to be codified at 47 U.S.C. § 208(b)(2)).

82. The US West Companies' arguments that the Bureau could not properly take any action with respect to the instant complaints because they present "novel questions of law" are equally unavailing. It is unnecessary to decide in this proceeding whether the Bureau has authority to consider such questions because no novel questions were addressed in the Bureau's orders. The Commission's authority to prescribe a common carrier's rate of return is well-established.[96] In addition, the Court of Appeals in *AT&T v. FCC* and *New England Telephone* specifically recognized the right to a statutory remedy when a carrier's interstate earnings have exceeded the maximum rate of return prescribed by the Commission.[97] It is clear that any question regarding the authority of the Commission to enforce a valid rate of return prescription has long been settled by the Commission and the courts. Thus, it cannot be said that the Bureau considered "novel" questions of law. Moreover, this issue is moot in view of our actions in this order, which is not a reconsideration of the Bureau's orders but is, instead, a determination by this Commission on the record of this proceeding.

83. The defendants also claim that the Bureau improperly shifted the burden of proof by requiring them to submit calculations of the amount of their overearnings, and that due process and the Administrative Procedure Act require that MCI's complaints be set down for hearing before an administrative law judge.

84. The defendants have provided no persuasive authority in support of their claim that they are entitled automatically to a hearing before an administrative law judge to resolve questions concerning damages. Section 208 of the Act does not mandate any particular form of procedure in complaint cases. When Section 208 is con-

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[96] *See Nader v. FCC*, 520 F.2d 182, 199-205 (D.C. Cir. 1975).

[97] *New England Telephone and Telegraph Co. v. FCC*, 826 F.2d at 1106-09; AT&T v. FCC, 836 F.2d at 1392.

strued in conjunction with the Act's general procedural authorization in Section 154(j), it is abundantly clear that the decision of when trial-type hearings are necessary under Section 208 is one which lies within the discretion of the Commission, or by the Bureau pursuant to delegated authority.[98] With respect to constitutional due process, there are no material disputed questions of fact at this stage of these proceedings; the issues are legal, not factual, in nature.[99]

85. Moreover, while we agree with the defendants' assertion that MCI bears the burden of proof in these proceedings, we reject the claim that they cannot be ordered in a complaint proceeding to provide evidence bearing on the amount of damages. It is well settled that defendants in a complaint proceeding may be required to produce such evidence where the complainant has made a *prima facie* showing of a violation and where the relevant information for measuring actual injury is solely within the possession or control of the defendants.[100]

86. It is not necessary, however, to resolve the question whether the Bureau was acting lawfully in the show cause orders by ordering the defendants to produce evidence bearing on damages relating to MCI complaints, or any other question raised by the defendants and MCI regarding damages. MCI's complaint contains allegations that

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[98] *See, e.g.*, Comark Cable Fund III, 100 FCC 2d 1244, *recon. denied*, 103 FCC 2d 600, *temporarily stayed*, 104 FCC 2d 451 (1985), *remanded for clarification sub nom.* Northwestern Indiana Telephone Co. v. FCC, 824 F.2d 1205 (D.C. Cir. 1987), *clarified on remand*, 3 FCC Rcd 3096 (1988), *pet. for review denied*, 872 F.2d 465 (D.C. Cir. 1989), *pet. for rehearing or rehearing en banc denied* (D.C. Cir. June 27, 1989).

[99] *See Northwestern Indiana Telephone Co. v. FCC*, 824 F.2d 1205 (D.C. Cir. 1987).

[100] *See Hughes Sports Network*, 38 FCC 2d 1052, 1054 (1972); *see also Intercambio, Inc.*, 3 FCC Rcd. 7247, 7260 n.49 (1988); *Peoples Telephone Cooperative*, 62 FCC 2d 113, 116 (1976).

identify with reasonable certainty the amount of damages for which recovery is sought. It has reserved its right under our rules to file a separate complaint to plead and prove such damages. We will, therefore, reserve judgment on damage issues until both the complainant and the defendants have the opportunity to address these issues and establish a full record on which we can base a judgment. In this order, we do no more than render judgment for MCI on the merits of its original complaint. We find that the defendants have violated the Communications Act by earning in excess of a valid rate of return prescription, thereby making their rates unjust and unreasonable under Section 201 of the Communications Act and themselves liable for such damages as MCI can demonstrate. Pursuant to our rules, MCI is entitled, within 60 days after public notice of this decision on the merits, to file a supplemental complaint concerning damages.

V. ORDERING CLAUSES

87. Accordingly, IT IS ORDERED, pursuant to Sections 4(i), 4(j), 201 and 208 of the Communications Act, as amended, that the above-captioned Complaints filed by MCI Telecommunications Corporation ARE GRANTED to the extent indicated herein.

88. IT IS FURTHER ORDERED, that the cross-complaints filed by the US West Carriers ARE DISMISSED.

89. IT IS FURTHER ORDERED, that MCI, in accordance with the Commission's rules, *see* 47 C.F.R. § 1.722, may file supplemental complaints concerning damages within 60 days after public notice of this decision.

FEDERAL COMMUNICATIONS COMMISSION

DONNA SEARCY
Secretary

APPENDIX C

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

IN THE MATTER OF
MCI TELECOMMUNICATIONS CORPORATION,
Complainant,

v.

File No. E-88-46S

PACIFIC BELL TELEPHONE COMPANY,

File No. E-88-44S

PACIFIC NORTHWEST BELL TELEPHONE COMPANY,

File No. E-88-51S

MOUNTAIN STATES TELEPHONE AND
TELEGRAPH COMPANY, and

File No. E-88-54S

NORTHWESTERN BELL TELEPHONE COMPANY,
Defendants.

MEMORANDUM OPINION AND ORDER

Adopted: January 29, 1993; Released: February 8, 1993

By the Commission:

I. INTRODUCTION

1. In this Memorandum Opinion and Order, we award damages to complainant, MCI Telecommunications Cor-

poration (MCI), for defendants'[1] violations of the Commission's rate of return prescription for the period October 1, 1985 through December 31, 1986 for the reasons and to the extent indicated below. In addition, we affirm the Common Carrier Bureau's determination that MCI may properly seek damages on behalf of its subsidiary, Satellite Business Systems, for defendants' rate of return violations. As also discussed below, we grant MCI's request for interest on the damages awarded here.

II. BACKGROUND

2. On January 9, 1990, the Commission issued a Memorandum Opinion and Order in the above-capitioned proceedings finding that MCI had met its burden of establishing that the defendant local exchange carriers (LECs) had violated Section 201(b) of the Communications Act of 1934, as amended (the "Act"), 47 U.S.C. § 201(b), by earning in excess of the rate of return prescribed by the Commission for the period October 1, 1985 through December 31, 1986.[2] In so ruling, the Commission rejected various arguments raised by the defendants to support their claims that allegations of earnings in excess of a prescribed rate of return fail to state a cause of action for damages under the Act. The Commission also concluded that the decision of the U.S. Court of Appeals in *American Telephone and Telegraph Company v. FCC*[3] does not

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[1] Defendants are Pacific Northwest Bell Telephone Company (PNB), Mountain States Telephone and Telegraph Company (MTN), and Northwestern Bell Telephone Company (NWB) (collectively "USWC") and Pacific Bell Telephone Company (Pacific Bell).

[2] MCI Telecommunications Corporation v. Pacific Northwest Bell Telephone Co., *et al.*, 5 FCC Rcd 216 (1990) (*MCI Liability Order*), *recon. denied*, 5 FCC Rcd 3463 (1990), *appeal dismissed sub nom.* Mountain States Tel. and Tel. Co., *et al.* v. FCC, 951 F.2d 1259 (10th Cir. 1991) (per curiam).

[3] 836 F.2d 1386 (D.C. Cir. 1988) (*AT&T v. FCC*).

preclude an award of damages based on earnings in excess of a prescribed rate of return.[4] The Commission also rejected: (a) arguments by some defendants that the rates in effect during the period in question were effectively prescribed by the Commission and, therefore, could not be subject to retroactive reduction through an award of damages; (b) claims by all the defendants that Section 415 of the Act barred all or portions of MCI's complaints: [5] and (c) defendants' assertions of procedural irregularities in the Bureau's and Commission's handling of the complaints.[6]

3. In finding that the defendants had violated the Act by earning in excess of the prescribed rate of return, the Commission further held that the defendants are liable for damages to the extent that the complainant can establish that it was damaged as a result of the violations.[7] The Commission, noting that MCI had properly reserved the right to file supplemental complaints for damages pursuant to Section 1.722 of the Commission's rules,[8] directed MCI to file such complaints within sixty days from release of the liability orders if it wished to pursue its damages claims.[9] On March 12, 1990, MCI filed supplemental complaints for damages on behalf of itself and its subsidiary

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[4] *See MCI Liability Order*, 5 FCC Rcd at 221-23, paras. 45-60.

[5] *See* 47 U.S.C. § 415. Subsection 415(b) provides in pertinent part that "[a]ll complaints against carriers for the recovery of damages not based on overcharges shall be filed with the Commission within two years from the time the cause of action accrues, and not after . . . ." The term "overcharges" is defined in subsection 415(g) to mean "charges for services in excess of those applicable thereto under the schedules of charges lawfully on file with the Commission."

[6] *MCI Liability Order*, 5 FCC Rcd at 225-26, paras. 79-86.

[7] *Id.* at 217, para. 62.

[8] 47 C.F.R. § 1.722.

[9] *MCI Liability Order*, 5 FCC Rcd at 223, para. 61.

Satellite Business Systems.[10] The defendants have filed answers, motions to dismiss, a motion for summary judgment and related pleadings in which they dispute the complainant's damages claims.[11]

4. On May 11, 1992, the Common Carrier Bureau (Bureau) released an order resolving outstanding discovery disputes and establishing further discovery and briefing schedules.[12] USWC has also filed an application for review

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[10] MCI reached a negotiated settlement with one of the defendants prior to filing a supplemental complaint and the proceeding was dismissed on joint motion of the parties to that proceeding. *See* MCI Telecommunications Corp. v. Southwestern Bell Telephone Co., 5 FCC Rcd 4566 (Enf.Div.Com.Car.Bur. 1990). MCI subsequently reached settlement with other LECs and those cases have also been dismissed on joint motion of the parties. *See* MCI Telecommunications Corp. v. Michigan Bell Telephone Co., 5 FCC Rcd 4569 (Enf.Div.Com.Car.Bur. 1990); MCI Telecommunications Corp. v. Wisconsin Bell, 5 FCC Rcd 4567 (Enf.Div.Com.Car.Bur. 1990).

[11] Defendants have filed numerous motions to dismiss, as well as a motion for summary judgment in these proceedings as follows: USWC filed a Joint Motion to Dismiss on March 31, 1988, a Joint Supplemental Motion to Dismiss Complaint for Damages on April 11, 1990, and a Supplement to Motion to Dismiss on February 14, 1992. Pacific Bell filed a Motion to Dismiss on March 31, 1988, a Motion to Dismiss Supplemental Complaint on April 25, 1990, and a Motion for Summary Judgment on January 17, 1992. MCI opposed each of these motions. Pacific Bell filed replies in all instances. USWC filed replies except to the opposition to its March 1988 motion to dismiss. The motions to dismiss and motion for summary judgment are dismissed consistent with our rulings herein.

[12] MCI Telecommunications Corporation v. Pacific Bell Telephone Co., *et al.*, 7 FCC Rcd 2985 (Comm.Car.Bur. 1992) (*Discovery Order*). USWC served interrogatories on MCI to which MCI responded on June 5, 1992 with a supplemental response on July 2, 1992. MCI filed its brief on July 6, 1992 (MCI Br.), Pacific Bell filed its brief on June 30, 1992 (Pacific Bell Br.), and USWC filed its brief on July 2, 1992 (USWC Br.). MCI filed its reply brief on July 14, 1992 (MCI RBr.), Pacific Bell filed its reply brief on July 10, 1992 (Pacific Bell RBr.), and USWC filed its reply brief

of the *Discovery Order* seeking reversal of the Bureau's determination that Satellite Business Systems (SBS), a subsidiary of MCI, is encompassed by MCI's damages complaints. Pursuant to the *Discovery Order*, the parties submitted their initial briefs and reply briefs setting forth their respective claims and arguments.[18]

III. THE COMPLAINTS FOR DAMAGES

5. MCI's damages claims rest primarily on the contention that the proper measure of damages it incurred as a result of the defendants' rate of return prescription violations is the difference between the amounts it actually paid the defendants for interstate access services during the October 1, 1985 through December 31, 1986 monitoring period and the amount it would have paid if the defendants' rates produced earnings that did not exceed the Commission's prescription. The defendants, however, have raised a number of challenges to MCI's damages claims, including a number of arguments that were previously considered and rejected by the Commission in the

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on July 13, 1992 (USWC RBr.). MCI filed unopposed motions for leave to file its brief and reply brief out of time. We will grant the motions and accept both filings.

[18] As a preliminary matter, we note that USWC has stated that it filed its brief directly with the Commission because it could find no order delegating damages authority to the Bureau. In addition, USWC formally objects if the Bureau is deciding these cases under delegated authority because it contends that the Bureau has been performing investigative and prosecutorial functions in these proceedings and cannot, under Section 554(d) of the Administrative Procedure Act (5 U.S.C. § 554(d)), act as decision maker herein. USWC Br. at 2, n.5. While we agree with USWC that the damages issue must be decided by the Commission, 47 U.S.C. § 155(c)(1), the Bureau may deal with interlocutory matters such as discovery issues. We also disagree with USWC's characterization of the Bureau's activities regarding these complaint proceedings. The Bureau has at all times been acting as the "decision maker" and not as an "investigator" or "prosecutor."

MCI Liability Order.[14] We address the parties' pertinent contentions below.

A. Satellite Business Systems (SBS)

1. Contentions of the Parties

6. As a threshold matter, we must decide whether MCI is entitled to seek damages on behalf of its subsidiary SBS. The Bureau found that MCI's damages claims properly encompass the claims of SBS and required defendants to submit information to MCI regarding SBS.[15] USWC filed an application for review of the Bureau's determination [16]

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[14] The issues and arguments raised by Pacific Bell and USWC in response to MCI's claims are identical in their essentials. For the sake of convenience and clarity, we will refer to defendants' arguments as if they are part of the same pleading. To the extent that individual defendants raise separate or unique arguments, we will address them separately.

[15] *Discovery Order*, 7 FCC Rcd at 2987. On May 26, 1992, in response to the *Discovery Order*, USWC filed an answer to MCI's first set of interrogatories in which it provided information to MCI regarding SBS. USWC amended its interrogatory answers on June 9, 1992. Pacific Bell filed, on May 26, 1992, a supplemental answer to MCI's interrogatories in which it states that it has no records of the total amount billed to SBS for interstate switched traffic sensitive access service for the 1985-1986 monitoring period. Pacific Bell states that all amounts billed to SBS were included in Attachments 1-4 to its Response to Order to Show Cause filed August 16, 1989.

[16] USWC filed its Application For Review on June 9, 1992 (Application). MCI filed an opposition to the Application on June 24, 1992 (MCI Opposition) and USWC replied on July 9, 1992. We note that Pacific Bell asserts in its reply brief that should MCI be awarded damages on behalf of SBS in this proceeding, any such damages award should be offset by undercharges to another MCI subsidiary, Telecom*USA, Inc., that has filed a separate complaint against Pacific Bell (File No. E-90-346, filed May 29, 1990). Pacific Bell states that it had not raised this issue before because it recently learned that Telecom*USA, Inc. is a subsidiary of MCI. Pacific Bell RBr. at 14.

arguing that the Bureau's ruling constitutes prejudicial error and is inconsistent with established law and the Commission's rules. To support its claim, USWC states that SBS was not a part of MCI during a substantial part of the 1985-1986 monitoring period and it was not named a party complainant in MCI's original complaints.[17] USWC points out that SBS was not transferred to MCI until February 14, 1986. Additionally, USWC states that MCI was the sole complainant in the original complaints and at no time has MCI filed a motion for leave to amend its complaints to include SBS as a complainant. USWC further argues that MCI's belated attempts to include SBS in the supplemental complaints for damages filed here fails all relevant legal tests.[18]

7. MCI admits that SBS was not part of MCI during a portion of the 1985-1986 monitoring period, but argues that as the current owner of SBS and its successor in interest, it is entitled to seek relief on SBS's behalf.[19] MCI points out that the Commission may waive its regulations for good cause either upon motion of a party or upon its own motion.[20] Accordingly, MCI contends that ". . . the lack of a formal motion to amend the complaint is, at worst, a technical flaw that is not fatal to the addition of SBS to MCI's damages claims."[21] MCI further asserts that case law supports the Bureau's finding that MCI may seek damages on SBS's behalf.[22]

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[17] Application at 4. USWC also argues, in its Joint Supplemental Motion to Dismiss, that we should dismiss MCI's claims on behalf of SBS. USWC Joint Supplemental Motion to Dismiss at 6. In addition, the parties address this issue in briefs and reply briefs filed herein. *See, e.g.*, USWC Br. at 19-22; MCI R.Br. at 43-44.

[18] *Id.* at 7; USWC Br. at 19.

[19] MCI Opposition at 2-3.

[20] *See* 47 C.F.R. § 1.3.

[21] MCI Opposition at 5.

[22] *Id.* at 7-14, citing to *Staren v. American National Bank & Trust Co*, 529 F.2d 1257 (7th Cir. 1976); *Gregg Comm. Systems,*

8. MCI rejects defendants' claims that its request for damages on behalf of SBS is barred under Section 415 of the Act and Section 1.722 of the Commission's rules. MCI argues that its underlying original complaint effectively encompassed SBS. MCI further states that even if its claims on behalf of SBS could be considered separate claims, such claims are proper because they relate back to the date of the original complaint for purposes of Section 415 of the Act and the Commission's rules.

9. USWC counters that MCI's failure to name SBS as a complainant is not a mere technical flaw or a formality. USWC contends that the recent decision in *Illinois Bell Tel. Co. v. FCC*[23] is instructive.[24] In that case the court found that the Commission had improperly applied new rates retroactively and ordered a refund without complying with the suspension procedures of Section 204(a)(1) of the Act. USWC argues, in effect, that the same principle should apply to MCI's failure to follow the necessary Com-

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Inc. v. AT&T, 98 F.R.D. 715 (N.D. Ill. 1983); *Issen v. GSC Enterprises*, 538 F. Supp. 745 (N.D. Ill. 1982); *De Franco v. United States*, 18 F.R.D. 156 (S.D. Cal. 1955); *Leachman v. Beech Aircraft Corp.*, 694 F.2d 1301 (D.C. Cir. 1982); *Warpar Mfg. v. Ashland Oil, Inc.*, 102 F.R.D. 749 (N.D. Ohio 1983); *EEOC v. Westinghouse Elec. Corp.*, 869 F.2d 696 (3d Cir. 1989), *remanded on other grounds*, 493 U.S. 801 (1989); and *EEOC v. Westinghouse Elec. Corp.*, 632 F. Supp. 343 (E.D. Pa. 1986).

The cases cited by complainant and defendants to support their claims regarding SBS deal with the construction and application of Section 15 of the Federal Rules of Civil Procedure (Federal Rules) pertaining to amendment of complaints. Although at times we find the Federal Rules to be instructive in handling certain proceedings, the Commission retains considerable discretion in fashioning its rules of practice and procedure and is not bound by the Federal Rules. *See, e.g.*, Amendment of Rules Governing Procedures to be Followed Where Formal Complaints are Filed Against Common Carriers, 3 FCC Rcd 1806, 1813, para. 57 (1988).

[23] 966 F.2d 1478 (D.C. Cir. 1992) (*Illinois Bell*).

[24] USWC Br. at 21.

mission's rules and to the Bureau failure to enforce those rules.

2. Discussion

10. We find that the Bureau did not err when it allowed MCI's claims for damages on behalf of SBS. USCW's attempt to characterize SBS as a non-party to this damages proceeding is unavailing.[25] The defendants do not dispute that SBS took access services and paid rates that produced earnings levels at issue in these complaints. Nor do defendants dispute MCI's dominion over SBS at the time it filed its complaint or that MCI is the successor in interest to any claims that could otherwise have been asserted by SBS as a separate, independent entity. We agree with MCI that it was not required to specify in its original complaint each of its wholly-owned subsidiaries through whom tariffed services were purchased from defendants.[26] MCI's original complaint alleged unlawfully high rates and the services purchased by SBS from defendants clearly fall within the scope of the defendants' misconduct. MCI's claims on behalf of SBS go not to the question of liability, but the amount of damages suffered as a consequence of defendants' actions.[27] We conclude, therefore, that MCI has properly placed the claims of its subsidiary, SBS, before the Commission.[28]

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[25] According to USWC, "Section 1.722(b) of the rules gives the same complainant the right to seek damages in a supplemental complaint, but nowhere does it provide for the rights of *non parties* to seek damages in the same complaint proceeding." Application for Review at p. 8, n.32, (emphasis in original).

[26] MCI Br. Appendix C at 6.

[27] USWC's attempts to distinguish the court precedents cited by MCI to support its claims that SBS is properly encompassed by its complaint are simply not persuasive. *See* Application for Review at pp. 10-12.

[28] Defendants' reliance on *Illinois Bell* is misplaced because that decision centered on what the court perceived as the Commission's

B. Liability For Damages

1. Contentions of the Parties

11. Defendants raise a number of arguments to support their claims that they cannot be held liable for damages based solely on the fact that their rates produced earnings in excess of the Commission's prescribed rate of return. For the most part, these arguments were considered at length and rejected in the *MCI Liability Order* and require no further discussion here.[29] Defendants make the additional argument that the decision in *Ohio Bell Telephone Company v. FCC*,[30] issued after the release of the *MCI Liability Order*, requires dismissal of MCI's complaints.[31] According to the defendants, *Ohio Bell* reaffirms the proposition established in *AT&T v. FCC* that the Commission cannot order refunds for carrier overearnings without allowing the carrier to re-coup or off-set underearnings,[32] nor may the Commission order refunds on an individual operating company basis without taking into account total

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failure to follow statutorily prescribed procedures in effecting refunds under Section 204(i) of the Act.

[29] *MCI Liability Order*, 5 FCC Rcd at 220-225. The Commission held that the defendants have violated the Act by earning in excess of a valid rate of return prescription, thereby making their rates unjust and unreasonable under Section 201 of the Act and themselves liable for such damages as MCI can demonstrate. In effect, we have previously determined that defendants' rates were unjust and unreasonable to the extent such rates produced earnings in excess of prescribed levels. To pursue a claim for damages in these proceedings, MCI need only show that it took service in the access service categories in which defendants overearned and set forth the manner and the extent to which it was damaged as a result of paying defendants' unlawfully high rates.

[30] 949 F.2d 864 (6th Cir. 1991) (*Ohio Bell*).

[31] USWC Supplement to Motion to Dismiss at 3-5; Pacific Bell Motion for Summary Judgment at 1 and 7.

[32] Pacific Bell Motion for Summary Judgment at 8-9.

company earnings.[33] Defendants contend that these propositions are not narrowly confined to the Commission's rate-making activities under Sections 204-205 of the Act[34] but are equally applicable when the Commission decides private complaints for damages under Section 208 of the Act.

12. MCI counters that, like *AT&T v. FCC, Ohio Bell* involved a Commission order under its public rate-making authority, which must satisfy the "end result" test set forth in *Federal Power Commission v. Hope Natural Gas Co.*[35] MCI argues that individual complaints for damages are not subject to the "end result test" articulated in *Hope*. MCI points out that the court in *AT&T v. FCC* stated that "an agency rate order 'viewed in its entirety' must produce a just and reasonable 'total effect' on the regulated business."[36] In addition, the court was dealing with the industry-wide application of the automatic refund rule as a whole over the long run. According to MCI, it was the operation of the refund rule in its entirety that was unreasonable. MCI further argues that this proceeding is not equivalent to the refund rule governing all overearnings; rather, it is an individual complaint by MCI for damages caused by the defendants' overearnings.[37] MCI contends that *Ohio Bell* simply applied *AT&T v. FCC* to another Commission public enforcement proceeding, and the court's reasoning is inapplicable to private Section 208 damages claims.[38]

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[33] USWC Supplement to Motion to Dismiss at 3-4.

[34] 47 U.S.C. §§ 204-205.

[35] 320 U.S. 591 (1944) (*Hope*).

[36] MCI Opposition to Supplement to Motion to Dismiss at 7, citing to *AT&T v. FCC*, 836 F.2d at 1391-92.

[37] *See, e.g.*, MCI Opposition to Supplement to Motion to Dismiss at 8-9.

[38] *Id.*

2. Discussion

13. Contrary to defendants' contentions, *Ohio Bell* does not undermine our decision in the *MCI Liability Order* that a complainant/customer may recover damages if it can establish that a carrier from whom it purchased service has violated a valid rate of return prescription and that the complainant/customer suffered damages as a result of the violation. In *Ohio Bell* the court found, as in *AT&T v. FCC,* that any requirement that carriers refund earnings in execss of a prescribed rate of return that failed to take into account a carrier's underearnings, appeared to be inconsistent with the Commission's own understanding of its rate of return prescription.[39] The court's reasoning was apparently based on its belief that the Commission considered a rate of return prescription to establish both minimum and maximum limits on the earnings levels of the affected carriers.[40] The Commission, however, recently clarified its position that a rate of return prescription is not a minimum, but rather a point within a broad zone of reasonableness:

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[39] *Ohio Bell,* 949 F.2d at 874.

[40] 949 F.2d at 872-873. In *AT&T v. FCC,* the court stated that

> . . . the Commission has authority under the Act to order refunds where a carrier has violated an outstanding rate-of-return prescription. That authority must however, be exercised in a way that does not contradict the Commission's own theory of rate of return regulation.

AT&T v. FCC, 836 F.2d at 1392. The court set aside the automatic refund rule adopted by the Commission in Authorized Rates of Return for the Interstate Services of AT&T Communications and Exchange Telephone Carriers, CC Docket No. 84-800, Phase I, FCC 85-527 (released Sept. 30, 1985), 50 Fed. Reg. 41,350 (Oct. 10, 1985), *modified on reconsideration,* Memorandum Opinion and Order, FCC 86-114 (released March 24, 1986), 51 Fed. Reg. 11,033 (Apr. 1, 1986), *further recon. denied,* 2 FCC Rcd 190 (1987). The court found the automatic refund mechanism to be arbitrary and capricious "because it is inconsistent with the rate of return prescription it purports to enforce." *AT&T v. FCC,* 836 F.2d 1386, 1390.

We acknowledge that the Commission may not have made its understanding of the rate of return it prescribes sufficiently clear in prior orders. However, subsequent to the [decision in *AT&T v. FCC*], we emphatically explain our position:

> 'In light of the ruling in [*AT&T v. FCC*], in which the Court of Appeals determined that our automatic refund provision was at odds with our own understanding of our rate of return prescription, we wish to clarify that we do not view this prescription as both a maximum and a minimum.' That is, it does not represent a unique balance point such that '[i]f the rate were higher, the balance would tip in favor of the investor; if lower, it would tip in favor of the consumer.' Our accumulated experience with rate of return prescriptions . . . convince us that there is no such point. Indeed, even the lower boundary of our range of cost of capital estimates does not represent a bright line such that a company earning just below that level would be forced out of business. We believe there is a substantial gap between an earnings level that is fully adequate to assure attraction of captial on favorable terms, and an earnings level which, if sustained over time, would be confiscatory.' [41]

The Commission went on to emphasize that this point is "neither the maximum nor minimum necessary to meet

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[41] Amendment of Parts 65 and 69 of the Commission's Rules to Reform the Interstate Rate of Return Represcription and Enforcement Processes, CC Docket No. 92-133, Notice of Proposed Rulemaking and Order, 7 FCC Rcd 4688 (1992) (*NPRM & Order*) at 4701, para. 96 (footnotes omitted) citing to Represcribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers, CC Docket No. 89-624, Order, 5 FCC Rcd 7507 (1990) at 7532, para. 217, *recon. denied*, 6 FCC Rcd 7195 (1991), *appeal docketed sub nom. Illinois Bell Telephone Co., et al., v. FCC*, No. 91-1020 (D.C. Cir. Jan. 11, 1991).

constitutional standards."[42] Rather, the Commission stated, it is a point selected based on consideration of all relevant factors, within a zone that is narrower than the zone bounded on the lower end by the constitutional minimum.[43] Therefore, the concern raised by the court in *AT&T v. FCC*, and echoed in *Ohio Bell*, about inconsistencies in the Commission's rate of return theory have been satisfied in the Commission's subsequent rate of return proceedings.

14. In any event, we disagree with the defendants' claim that *Ohio Bell* and *AT&T v. FCC* compel us to dismiss MCI's complaints. As we emphasized in the *MCI Liability Order*, automatic refunds and refunds ordered under Section 204 of the Act are different from individual actions for damages under Section 208. Unlike the automatic refund mechanism in *AT&T v. FCC* or the refund procedure in *Ohio Bell*, both of which resulted from rulemaking proceedings initiated at the Commission's discretion, individual actions for damages under Section 208 are initiated by private parties seeking damages for injuries to themselves; those private parties have the burden of establishing both a violation of the Act and actual injury.[44] The courts in *AT&T v. FCC* and *Ohio Bell* did not discuss private complaints for damages; they did not invalidate private actions for damages; and their analysis is not applicable to the different separately authorized complaint procedure set forth in Sections 206-209. Accordingly, those decisions do not require us to depart from our holding in the *MCI Liability Order* that defendants have violated the Communications Act by earning in excess of a valid rate of return prescription, thereby making their rates unjust and unreasonable under Section 201 of the Communications Act and themselves liable for damages to the extent a

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[42] *NPRM & Order*, 7 FCC Rcd at 4701, para. 97.

[43] *Id.*

[44] *See MCI Liability Order*, 5 FCC Rcd at 222-23, para. 55.

complainant/customer can establish that it was damaged as a result of the violation.[45]

C. Damages and Interest Claims

1. Damages

a. Contentions of the Parties

15. As referenced above, MCI's damages claims rest primarily on the contention that the proper measure of the damages it incurred as a result of defendants' violations is the difference between the amount it actually paid defendants for interstate access services during the October 1, 1985 through December 31, 1986 period and the amount it would have paid if the defendants' rates had produced earnings that did not exceed the Commission's prescribed rate of return.[46] In the *Discovery Order*, the Bureau stated that it tended to agree, in principle, that a possible measure of the damages stemming from defendants' rate of return violations could be that difference.[47] The Bureau was not persuaded on the record before it, however, that a damages determination based solely on such a measure necessarily reflected actual damages incurred by MCI.[48] The defendants were invited to submit evidence that could serve to mitigate or otherwise reduce MCI's damages claims. Specifically, the Bureau stated that evidence that would show that

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[45] *Id.* at 226, para. 86.

[46] In support of what it characterizes as the traditional approach to damages, MCI cites to *Southern Pacific Co. v. Darnell-Taenzer Co.*, 245 U.S. 531 (1918) (*Darnell-Taenzer*), which MCI states construed the cognate provisions of the Interstate Commerce Act (ICA), and the cases that followed this decision. In *Darnell-Taenzer*, the Court upheld an Interstate Commerce Commission (ICC) order requiring a carrier to pay reparations to a shipper in the amount that the rate charged by the carrier exceeded a rate found reasonable by the ICC.

[47] *Discovery Order*, 7 FCC Rcd at 2987, para. 12.

[48] *Id.*

MCI's share of excessive earnings realized in a particular access category by a defendant could be offset or otherwise reduced due to facts and circumstances surrounding MCI's purchase of other interstate access services from such defendant for the relevant monitoring period might be relevant.[49]

16. Under what it describes as the "traditional" damages approach, MCI states that it should be awarded damages of $2,210,851 from Pacific Bell and $2,322,960 from USWC, exclusive of interest.[50] MCI states that the data underlying these calculations were taken from the defendants' Forms 492, their responses to discovery and other filings in these proceedings as well as from published tax tables.[51] To derive the stated amounts, MCI calculated, for each study area and access service category in which a defendant's earnings exceeded the rate of return prescription of 12.75% plus .50% buffer, the overall percentage that the service rates in that category should have been reduced in order to yield earnings of no more than 13.25%. The resulting percentage represents the rate reduction percentage used by MCI in its computations. MCI then took MCI's and SBS' combined shares of the total industry usage of each service category in each study area in which a defendant overearned and calculated its actual payment for each service category and each study area. MCI then applied a "rate adjustment factor" (1 minus the rate reduction percentage) to the amount it actually paid to derive the amount it would have paid if defendant had not overearned.[52] MCI also claims interest calculated at the Internal Revenue Service (IRS) rate from the month that each excess payment

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[49] *Id.*

[50] This amount includes $926,058 from NWB, $1,134,175 from MTN, and $262,727 from PNB.

[51] MCI Br. at 11-12.

[52] *Id.* at 12-15.

was made.[53] MCI contends it is entitled to interest on the damage amounts which, through July 30, 1992, totals $1,947,537 in the case of Pacific Bell and $2,046,105 in the case of USWC.[54]

17. The defendants challenge MCI's damages claims on a number of grounds, raising several arguments that were previously considered and rejected by the Commission in the *MCI Liability Order*. Defendants contend that by simply basing its damages claims on a calculation of MCI's prorated share of category-level overearnings, MCI asks the Commission to award it damages in the same amounts it would have received under the automatic refund rule invalidated by the court in *AT&T v. FCC*.[55] The defendants maintain that such a result is expressly precluded by *AT&T v. FCC*. The defendants add that the decision in *Ohio Bell* precludes an award of damages based solely on category level overearnings. Defendants also contend that the decision in *Illinois Bell* precludes an award of damages for past overearnings because that decision limits the Commission to ordering prospective relief under Section 205 of the Act.[56]

18. Defendants next contend that, even if *AT&T v. FCC* and *Ohio Bell* do not preclude MCI's damages claims, the claims still fail because MCI's complaints do not establish a valid cause of action. According to defendants, to pursue a damages claim, MCI must first show that the defendants charged unjust and unreasonable rates for interstate access services during the period

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[53] *Id.* at 15.

[54] MCI RBr. at 46-47 and Appendix D. MCI states that it computed interest at the IRS quarterly interest rate, compounded daily, beginning May 15, 1986 and ending July 30, 1992.

[55] *See, e.g.*, Pacific Bell Br. at 7; USWC Br. at 5, 7-9. In addition, defendants contend that *Ohio Bell* makes clear that it was the end result of the automatic refund mechanism, not the mechanism itself, that was unlawful. Pacific Bell Br. at 9.

[56] *See, e.g., id.* at 7.

in question, not that defendants' rates produced excessive returns in individual service categories.[57] Moreover, defendants argue, Section 206 of the Act [58] requires MCI to prove injury, causation, and the amount of damages in addition to establishing a violation of the Act.[59] Defendants maintain that by simply referencing defendants' earned rates of return for individual access service categories, MCI has not only failed to allege any facts that would establish that defendants' rates were unjust and unreasonable during the period in question but has also failed to show that it sustained actual damage as a result of those rates.[60]

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[57] USWC argues that MCI must specify an identifiable rate that MCI paid that was too high or too low. USWC Br. at 10. In addition, USWC cites to a 1970 circuit court decision to support its claim that where retroactive relief is ordered for rates paid pursuant to a tariff that is subsequently found unjust and unreasonable, the Commission must determine what a just and reasonable rate is. *Id.*, citing to *Middlewest Motor Freight Bureau v. United States*, 433 F.2d 212, 232 (8th Cir. 1970) (*Middlewest*), *cert. denied*, 402 U.S. 999 (1971). USWC's reliance on *Middlewest* is misplaced. *Middlewest* dealt with the question of restitution (not damages) to shippers for charges collected by carriers during the pendency of an injunction improperly issued by a district court against an ICC order, which had found the carriers' rates to be unlawful. The circuit court found the injunction to be improperly issued and ordered restitution by the carriers for higher charges collected while the injunction remained in effect. In discussing the difference between overcharges, reparations, and restitution the court pointed out that, in the context of reparations, the agency, and not the court, must determine the just and reasonable rate when filed rates are found to be unjust and unreasonable. The *Middlewest* decision thus focused on restitution under very narrow circumstances—restitution for higher charges collected by carriers despite a determination by the expert agency charged with regulating the rates that the rates were unlawful.

[58] *See* 47 U.S.C. § 206.

[59] *See, e.g.*, Pacific Bell Br. at 11.

[60] *See, e.g., id.* at 10-11; USWC Br. at 11-12. USWC contends that the principle that MCI must still prove it was damaged and

19. The defendants each raise distinct arguments to support their claims that an award of damages to MCI based on carrier overearnings is inappropriate for equi-

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in what amount was established by the Supreme Court in *Southern Ry. Co. v. Seaboard Allied Milling Corp.*, 442 U.S. 444, 454-55 (1979) (*Seaboard*), *reh'g denied*, 444 U.S. 890 (1979), in construing relevant sections of the ICA. The Court stated:

> [O]ur sole concern is the Commission's decision not to investigate under § 15(8)(a) [204], a decision that has only two final consequences. First, the burden of proof with regard to *reasonableness* is placed on the shipper under § 13(1) [208] rather than on the carrier, who would have borne it in a § 15(8)(a) [204] proceeding. (With respect to all other aspects of lawfulness, however, the burden is borne by the shipper in both proceedings.) Second, the shipper's relief, if unlawfulness is proved, is limited under § 13(1) [208] to actual damages rather than the full refund of overcharges available under § 15(8)(a) [204].

USWC states that this ruling has been found applicable to proceedings under the Communications Act. *See Aeronautical Radio, Inc. v. FCC*, 642 F.2d 1221, 1235 n.35 (D.C. Cir. 1980) (*ARINC*), *cert. denied*, 451 U.S. 920 (1981). Here too, USWC's reliance on case precedent is misplaced. In *Seaboard*, the Court dealt with the narrow question of whether there must be judicial review of the ICC's decision not to conduct a Section 15(8)(a) investigation of a tariff. The Court held that judicial review was inappropriate because the shippers could pursue individual complaints under Section 13(1) of the ICA and the decision not to investigate under Section 15(8)(a) did not prejudge the lawfulness of the tariff. As the Court noted, the ICC's decision not to investigate had only two consequences—the burden to establish reasonableness is shifted from the carrier to the shipper and the shipper might not be entitled to the full amount of the overcharge because it must prove actual damages. *Seaboard*, however, does not stand for the proposition that refunds for overcharges and an award of damages are always necessarily two different amounts. In fact, the Court acknowledges these amounts may be identical. *See* 442 U.S. 444, 455, n.8.

The Court of Appeals decision in *ARINC* similarly dealt with the reviewability of a Commission decison to accept a tariff. The court held that such action by the Commission is unreviewable since parties claiming to be aggrieved by the Commssion's acceptance of a tariff may avail themselves of the statutory complaint

table and policy reasons. USWC vigorously argues that MCI is actually seeking restitution or a refund of tariffed charges, not damages. USWC argues that regardless of how MCI characterizes the relief it seeks, any form of refund or restitution to MCI would be contrary to the public interest.[61] USWC further contends that an award of damages would be inequitable because (i) USWC's total corporate rate of return would be driven below the confiscatory level; (ii) there was uncertainty surrounding the tariff filings during the relevant period; and (iii)

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procedure in Section 208 of the Act. The court echoed the Supreme Court's ruling in *Seaboard* that the burden is on the complainant in an individual complaint action, and the amount of damages may not necessarily be the same as the amount received had the Commission investigated the tariff, found the rates to be unreasonable, and ordered refunds.

[61] USWC Br. at 13-19. USWC argues MCI must plead its case in equity and the Commission may only award a refund if we find that the public interest will be served by a refund award to MCI. USWC contends that the leading case in this area is *Moss v. Civil Aeronautics Board*, 521 F.2d 298 (D.C. Cir. 1975) (*Moss*), *cert. denied sub nom. Roberts v. Civil Aeronautics Board*, 424 U.S. 966 (1976), *reh'g denied*, 425 U.S. 966 (1976). USWC states that the refund in *Moss* "was governed by the equitable principles governing the law of restitution." USWC Br. at 14, citing to *Moss*, 521 F.2d at 304. Once again USWC's reliance on a court ruling is misplaced. *Moss* dealt with a claim for restitution by airlines passengers for fares paid pursuant to an order of the Civil Aeronautics Board (CAB) later found procedurally infirm by the court. The court had previously held that fares charged by the airlines pursuant to the CAB order were unlawful because the CAB had not complied with the requirements of the Federal Aviation Act in determining such rates. *See Moss v. CAB*, 430 F.2d 891 (D.C.Cir. 1970). The CAB, at the time of *Moss*, lacked any express reparations (damages) or refund power. The court noted that ". . . recovery can only be had in terms of restitution grounded in equitable considerations." 521 F.2d at 314. We are not limited herein to restitution because the Commission has express statutory authority to award damages, which is embodied in Sections 206-209 of the Act. The equity concerns discussed by the court in *Moss* are simply inapplicable to these individual damages complaints.

MCI would receive a windfall that would be inconsistent with sound equitable principles.[62]

20. For its part, Pacific Bell argues that MCI's claim for damages is flawed because MCI simply assumes that lower rates would have produced lower earnings[63] and offers no probative evidence to show what a reasonable rate would have been or to otherwise support its damages claims. Pacific Bell argues, as does USWC, that MCI would receive a windfall if it has passed the "overcharges" on to its customers and is now awarded damages.[64] Pacific Bell argues that had its access charges to MCI been lower in 1985-1986, it is almost certain that MCI's rates to its customers would have been lower.[65] Pacific Bell cautions the Commission to look at the "backdrop of the practical consequences" thereof and ensure that any decision granting MCI "refunds" is equitable under the circumstances.[66] Pacific Bell further argues that, should the Commission award damages to MCI, the Commission

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[62] USWC Br. at 16-19.

[63] For example, Pacific Bell alleges that had its rates been lower "it is almost a certainty" that MCI's rates to end users would have been lower also. Pacific Bell Br. at 14.

[64] *See, e.g., id.* at 13.

[65] *Id.* at 14. Pacific Bell cites to numerous newspaper and magazine articles to support this contention.

[66] *Id.* at 16, citing to *Las Cruces TV Cable v. FCC*, 645 F.2d 1041 (D.C. Cir. 1981) (*Las Cruces*). In *Las Cruces*, the court upheld, in part, and remanded, in part, a Commission decision requiring refunds under Section 204 of the Act. The court noted that *Las Cruces*

> is the first time that the Federal Communications Commission has attempted to articulate standards governing its award of refunds to customers of a communications common carrier under Section 204 of the Act.

645 F.2d at 1046. Pacific Bell's reliance on *Las Cruces* is unavailing, however, because equitable considerations that may impact a Section 204 investigation are not applicable in individual Section 208 complaint proceedings in which only damages are awarded.

should order MCI to pass the damages through to its end users in the form of a rate reduction.[67]

21. Finally, Pacific Bell argues that any award of damages to MCI based on overearnings should be reduced by Pacific Bell's underearnings in the common line category (earnings under 12.75%) and an automatic refund in the switched traffic sensitive category which Pacific Bell claims it made in 1988 prior to the court's decision invalidating the automatic refund rule.[68] Pacific Bell also contends that any damages awarded to MCI and SBS be offset by undercharges to another MCI subsidiary, Telecom*USA, Inc.[69] Taking these factors into consideration, Pacific Bell claims that MCI has already received a windfall of approximately three million dollars from undercharges which exceeds its damages claims. Therefore, Pacific Bell contends, equity dictates that MCI receive no damages in these proceedings.

22. MCI counters that defendants' threshold arguments regarding the effect of the court's ruling in *AT&T v. FCC* have largely been rejected or precluded by the *MCI Liability Order*. MCI states that the so-called similarities between its damages requests and the automatic refund do not "somehow transmogrify the private complaint remedy into a public enforcement refund remedy subject to entirely different standards and requirements" as alleged by the defendants.[70] MCI adds that defend-

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[67] Pacific Bell Br. at 16.

[68] *Id.* at 17-18.

[69] Pacific Bell RBr. at 14-15. We note that Telecom*USA, Inc. has filed a separate complaint against Pacific Bell and that at the time the separate complaint was filed, Telecom*USA, Inc. was not a subsidiary of MCI. *See* note 16, *supra*.

[70] MCI RBr. at 8. MCI also points out that the Sections 206-209 damages remedies are invulnerable to any challenge based on the decisions in *AT&T v. FCC* and *Ohio Bell*. This, MCI claims, is underscored by Judge Starr's concurring opinion in which he notes that refunds (under Section 204(a)) and damages (under Sec-

ants' arguments that it has failed to allege and prove violations of the Act and actual damage are unfounded because it has made a sufficient showing of each under traditional principles governing its statutory right to such relief. According to MCI, the only injury and causation it need show are the injury and causation arising from its payment of excessive rates for services it purchased from defendants during the relevant period. MCI maintains that it has shown that defendants charged it rates that produced earnings in excess of the Commission's prescribed rate of return and argues that its damages are the excessive charges that MCI paid. Those damages, MCI states, can easily be derived from the defendants' Forms 492 and the information that has been provided in these proceedings.[71] MCI states that it has calculated the percentages by which the overall rates in each service category and study area should be reduced to produce rates that did not overearn during the relevant monitoring period. Therefore, MCI asserts, it has proven damages under the traditional approach.[72]

23. MCI further argues that equitable considerations are relevant only to the Commission's public enforcement remedies and not to private complaints for damages because the Commission has no discretion in the award of damages under Sections 206-209 of the Act.[73] MCI states that Pacific Bell's equitable arguments regarding the failure of MCI to flow-through damages it might recover are also irrelevant to private complaint actions[74] and Pacific

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tions 206-209) are the two remedies specified in the Act for injured customers. *See AT&T v. FCC*, 836 F.2d at 1393-94. MCI also notes that Judge Starr also makes clear that a damages award does not constitute retroactive ratemaking in violation of the 'filed rate doctrine.' *Id.*

[71] *Id.* at 15.

[72] *Id.* at 16-17.

[73] *Id.* at 21.

[74] *Id.* at 26.

Bell cannot properly raise a "passing-on" defense.[75] MCI states that USWC has implicitly conceded that defendants' equitable defenses are germane only if MCI's claim is equitable in nature, i.e., a disguised claim for a refund or restitution under the Commission's public enforcement authority.[76] MCI reiterates that its claims are actions for damages under Section 206-209 of the Act, not for restitution or refunds.

24. MCI next argues that defendants' offset arguments should be rejected because the Commission has already held that cross-subsidies in earning categories are not allowed. Moreover, MCI claims, offsets are in the nature of counterclaims and as such, are not within the Commission's jurisdiction because they would involve the determination of a carrier's rights against a customer.[77] MCI adds that offsets would violate the "filed-rate doctrine" because defendants would, in effect, be allowed to recoup undercharges through retroactive rate adjustments as well as discriminate against those customers against whom such offsets were allowed.[78]

25. MCI further contends that Pacific Bell should not be given credit for its claimed partial refund of excess switched traffic sensitive charges in 1988.[79] MCI contends that Pacific Bell has not shown that MCI received a benefit from the switched traffic sensitive rate reduction. In any event, MCI argues, since Pacific Bell overearned

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[75] MCI argues that the press clippings cited to by Pacific Bell are insufficient to establish this defense. *Id.* at 28-29.

[76] *Id.* at 18.

[77] *Id.* at 33-35, citing to Thornell Barnes Co. v. Illinois Bell Telephone Co., 1 FCC Rcd 1247, 1275 (1965) (*Thornell Barnes*); Illinois Bell Telephone Company v. AT&T, 4 FCC Rcd 5628, 5270 at ¶ 17-18 (1989) (*Illinois Bell II*), *recon. denied*, 4 FCC Rcd 7759 (1989); *Pennsylvania R. Co. v. Fox & London, Inc.*, 93 F.2d 669 (2d Cir. 1938).

[78] MCI RBr. at 37-39.

[79] *Id.* at 42.

in this category in 1987-1988, the rate reduction is meaningless.

b. Discussion

26. *AT&T v. FCC and Ohio Bell:* The defendants' claims that the holdings in *AT&T v. FCC* and *Ohio Bell* control these proceedings and bar an award of damages to MCI are without merit for the reasons stated in the *MCI Liability Order*. We emphasized in that Order that the court in *AT&T v. FCC* explicitly acknowledged the Commission's authority to order a carrier to disgorge earnings in excess of a rate of return prescription,[80] finding only the remedy component of the Commission's rate of return prescription (the automatic refund mechanism) to be unlawful.[81] More to the point, we emphasized that "the [*AT&T v. FCC*] opinion does not address Section 208 complaint proceedings nor purport to alter the statutory scheme of the Act or the remedies Congress established therein."[82] The *Ohio Bell* decision, which relied in part on the reasoning in *AT&T v. FCC*, similarly does not address the Commission's authority to award damages in private complaint actions under Section 208 of the Act. *Ohio Bell* follows *AT&T v. FCC;* it does not expand upon its holding. In *Ohio Bell*, the court held that a Commission order requiring carriers to refund overearnings in the special access category under strategic-pricing guidelines for the 1985-86 and 1987-88 monitoring periods was arbitrary and capricious because the order

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[80] *AT&T v. FCC*, 836 F.2d at 1392 ("Thus, as we previously have concluded, the Commission has authority under the Act to order refunds where a carrier has violated an outstanding rate of return prescription").

[81] Indeed, the court in *Ohio Bell* recognized the continuing efficacy of our rate of return framework. *See* 949 F.2d at 868.

[82] *MCI Liability Order*, 5 FCC Rcd at 223, para. 56.

was inconsistent with the Commission policies establishing permissible rates of return.[83]

27. We also reject defendants' claim that the decision in *Illinois Bell* somehow leaves the Commission only with Section 205 authority in the face of a violation of our rate of return prescriptoin. In *Illinois Bell,* the court found that the Commission had ordered a refund under Section 204(a) of the Act without having issued a suspension order. The sole issue presented for resolution by the court was the difference in interpretation by the Commission and the petitioning parties of the Commission's authority under Section 204.[84] The court did not address individual complaint remedies, but merely held that the Commission is not authorized to order refunds under Section 204 without having issued a suspension order, and that in doing so it must have acted under Section 205, which provides for prospective relief only.[85] The defendants' claim that the *Illinois Bell* decision deprives the Commission of authority to award damages for violations of a valid rate of return prescription has no merit.

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[83] *See Ohio Bell,* 949 F.2d at 873. The court pointed out that

> [p]etitioners rely primarily on *A.T. & T. v. F.C.C.* . . . to argue that the Commission's order is arbitrary and capricious. *The case involved a refund order similar to the one in this case.*

949 F.2d at 872 (emphasis added).

[84] *Illinois Bell,* 966 F.2d at 1481.

[85] *Id.* at 1483. The court stated

> We conclude that when the FCC investigates and remedies an unreasonable rate which it has theretofore permitted to become fully effective without a suspension order, it acts under § 205, not § 204. We further conclude that the Commission has no authority under § 205 to order the refunds contemplated only under § 204.

Id. The court clearly did not limit or even address this Commission's authority to order damages in a Section 208 proceeding.

28. *Section 201(b) of the Act:* We turn now to the defendants' contention that MCI's damages claims must be dismissed because MCI has failed to prove defendants' rates were unjust and unreasonable within the meaning of Section 201(b) of the Act. These arguments were previously raised by the defendants in the liability phase of this proceeding. In the *MCI Liability Order*, we specifically held that MCI had met its burden of proof by establishing that the defendants had violated our rate of return prescription "thereby making their rates unjust and unreasonable under Section 201 of the Act." [86] Accordingly, the question before us now is not whether defendants' rates were unjust and unreasonable; rather the questions now are whether the complainant suffered any measurable damage as a consequence of paying rates previously determined by the Commission to be unlawful under Section 201(b).

29. The defendants next claim that even if MCI has sustained its burden and shown that defendants' rates were unjust and unreasonable, its damages claims must still fail because judicial precedent compels MCI to establish what a just and reasonable rate would have been as a prerequisite to pursuing damages claims based on unreasonable rates.[87] Defendants' claims in this regard are unavailing. We agree with the Bureau's determination in the *Discovery Order* that a proper starting point for assessing damages based on violations of a rate of return prescription is to look at the difference between the amount MCI paid for defendants' interstate access services and the amount it would have paid if defendants had charged rates that produced returns within the Commission's prescribed levels.[88] The issue in these proceedings it not whether individual rates are unlawful, but whether cumulative rates that produced earnings over and

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[86] *MCI Liability Order*, 5 FCC Rcd at 226, para. 86.

[87] USWC Br. at 10, citing *Middlewest*, 433 F.2d 212, 232.

[88] *See Discovery Order*, 7 FCC Rcd at 2987, para. 12.

above a prescribed rate of return are unjust and unreasonable. In emphasizing the Commission's authority under the Communications Act to prescribe and enforce carriers' rates of return,[89] we stated in the *MCI Liability Order* that

> [i]t does not disturb the balance of ratepayer and shareholder interests embodied in the Act to award damages to customers who demonstrate that they were injured by paying rates that resulted in a carrier earning in excess of its prescribed return. Even when a carrier operates under a prescription of a rate of return for broad categories, the carrier retains substantial flexibility in formulating rates. Carriers are permitted to make mid-course corrections if their actual return deviates from the authorized return. If actual earnings are higher than the authorized return, a carrier can file reductions and thereby avoid the risk of being ordered to pay damages. If actual earnings are below the authorized return, a carrier can file rate increases. Defendants had ample notice of our rules, which were developed in notice and comment Rule Making proceedings in which all of them participated, as well as the level of the prescription for each category. As a general matter, it would be inequitable to permit defendants, who were in the best position to set their rates at lawful levels in the first place, and who later had opportunities to correct those rates, to avoid responsibility for those unlawful rates, at the expense of their customers.[90]

MCI has shown that it purchased services from defendants at rates that produced earnings over and above the defendants' prescribed levels. The defendants, faced with the prospect of damages for violations of a binding rate of return prescription, cannot now so readily disavow

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[89] *MCI Liability Order*, 5 FCC Rcd 222-223.

[90] *Id.* at 223, para. 59 [footnotes omitted].

the substantial flexibility afforded carriers to achieve their authorized rate of return. In effect, the defendants would have us require MCI to do what defendants were neither required nor apparently able to do, that is establish the precise rates required to bring defendants' earnings within authorized levels for each of their interstate access service offerings. The defendants ask too much. The Commission's rate of return prescription, although it afforded carriers considerable leeway in setting their rates, bound the defendants to a maximum earnings limitation. We previously determined in the *MCI Liability Order* that a violation of such a prescription constitutes a violation of the Act for which damages may lie. It is appropriate and consistent with the Commission's rate of return regulatory scheme to inquire as to earnings in excess of prescribed levels for purposes of assessing damages claims.

30. *Damages and Offsets:* The defendants' arguments are devoted primarily to attempting to persuade the Commission that MCI's damages claims are really claims for restitution or refunds governed by equitable or public policy considerations. These considerations, according to defendants, militate against any award of damages to MCI based on excessive earnings. The defendants argue, in effect, that the damages MCI seeks are equivalent to refunds that would have been required under the refund mechanism invalidated by the court in *AT&T v. FCC*. We do not agree. We are concerned here with determining whether a particular customer, which has availed itself of a statutory complaint remedy under Title II of the Act, has sustained any measurable damage that can be traced to defendants' violations of the Act. Although a damages award under Section 208 of the Act might well be equal or substantially similar to a refund ordered under Section 204 of the Act,[91] this does not

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[91] *See Seaboard*, 442 U.S. 444, 445, n.8:

> If a shipper proves a rate is unreasonable and that he was damaged in the full amount he was overcharged, the outcome

transform a private complaint action into a public enforcement proceeding subject to broad public interest considerations.

31. We find defendants' arguments with respect to "passing-on" equally unavailing. MCI has made a claim for specific damages, and the defendants, in turn, may properly argue that they are entitled to certain offsets against those damages. Defendants, however, cannot simply make damages "go away" by alleging that MCI passed on the defendants' charges that led to excessive earnings to MCI's customers. Whether MCI passed on the overcharges or absorbed them does not alter the fact that the defendants overcharged MCI in violation of a binding rate of return prescription and must answer for for such violations. MCI clearly has a claim for damages because it had to pay more for service than it would have if defendants' rates had produced earnings at or within the Commission's prescribed levels. Even if MCI passed on the overcharges, it is very likely that MCI's sales to customers were adversely affected to the extent that its own rates were higher. The issue, however, is not what MCI has done in response to paying excessive rates, but whether MCI has been damaged as a result of these excessive rates.[92] In addition, MCI argues, and we agree, that the Commission's decision in *Hughes Sport Network, Inc.*[93] along with the Supreme Court's decision in

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of a 13(1) [§ 208] proceeding will be no different than that of a § 15(8)(a) [§ 204] proceeding in which the carrier fails to establish the reasonableness of the rate.

[92] In any event, while defendants have asserted that lower charges to MCI would have resulted in lower charges to MCI's customers, they have provided no persuasive evidence in support of this contention. Pacific Bell, for example, relies solely on press clippings that purportedly show that MCI's rates to its customers would have been affected by changes in defendants' rates. These clippings do not, however, establish, as a matter of law, that MCI, in fact, passed on defendants' overcharges to its customers.

[93] 34 FCC 2d 691 (*Hughes*), *recon. denied*, 38 FCC 2d 1052 (1972).

Darnell-Taenzer require that the "passing-on" defense be rejected. In *Hughes*, the Commission stated that

> the imposition of a charge which is unlawful because it is unreasonably high entitles the customer to reparation of the excessive amount without regard to whether or not the damages were passed on to other parties.[94]

Similarly in *Darnell-Taenzer*, the Court stated

> The only question before us is that at which we have hinted: whether the fact that the plaintiffs were able to pass on the damage that they sustained in the first instance by paying the unreasonable charge, and to collect that amount from the purchasers, prevents their recovering the overpayment from the carriers. The answer is not difficult. The general tendency of the law, in regard to damages at least, is not to go beyond the first step.[95]

32. Nor can we accept the defendants' related claim that we should require MCI to flow through any damages it may receive to its end user customers. Section 206-209 of the Act give private parties the right to file complaints challenging the acts or omissions of carriers and to recover monetary damages resulting from such acts or omissions. Complainants, however, are charged, as MCI is in the instant case, with the burden of establishing violations of the Act or Commission rule or order and the amounts or extent of damage suffered as a consequence of such violations. Accepting defendants' flow through argument would, in effect, transform MCI's complaints into class action suits on behalf of its customers, a result neither expressly contemplated by nor consistent with the private remedy created under Sections 206-209 of the Act.

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[94] *Id.* at 693.

[95] 245 U.S. at 533.

33. We also reject USWC's contention that a damages award to MCI is precluded because it would drive USWC's overall rate of return for USWC in the aggregate below the minimum necessary to raise capital and would further drive USWC's aggregated overall rate of return below confiscatory levels. Assuming *arguendo*, that such an inquiry is relevant to a Section 208 damages claim, USWC has failed to provide sufficient record evidence for the Commission to assess the impact of any damages award upon its overall interstate rate of return. While USWC has provided some data in Exhibits B and C to its brief,[96] it has made no clear showing of the amount by which an award to MCI would reduce its overall interstate earnings or rate of return let alone that any such reduction would be confiscatory. USWC's other equitable arguments regarding the uncertainty surrounding tariff filings during the 1985-86 period and an alleged windfall to MCI should it receive restitution are equally unavailing. First, USWC had the opportunity to make corrections to its tariff in order to assure that its earnings would not exceed the prescribed rate of return. USWC was not forced by the Commission to overearn during the relevant monitoring period. Second, MCI has shown that it paid unjust and unreasonable rates to the defendants, which entitles MCI to an award of damages to the extent indicated here. The consideration of whether such an award would result in a windfall to MCI has no place in the context of a Section 208 proceeding that, contrary to defendants' repeated assertions,

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[96] Exhibit B contains a summary and compilation of information submitted in MTN's, PNB's and NWB's Forms 492 for the relevant monitoring period, a calculation of how much money USWC would have earned if its entire carrier enterprise earned exactly at a 12.75% rate of return, and the same calculation at a 13.10% rate of return. Exhibit C contains a summary and compilation of USWC's over- and underearnings by rate element multiplied by MCI's market share to arrive at the dollar amount by which MCI over- or underpaid for element specific access services. USWC provided calculations at three rate of return levels—12.75%, 13.10%, and 13.25%.

is not governed by equitable principles. MCI has been damaged by defendants excessive earnings and, under legal principles, is entitled to an award of damages.

34. We also reject MCI's claim that the Commission has no jurisdiction to allow defendants to offset damage claims because it would, in effect, be a determination of a carrier's rights against a customer. MCI's reliance on *Thornell Barnes* and *Illinois Bell II* for this proposition is misplaced. *Thornell Barnes* involved a carrier's request to "set-off" overcharges billed to a customer for certain calls with purported undercharges on certain other calls. The Review Board disallowed the request because "it would involve a determination of the carrier's rights against a subscriber, over which the Commission has no jurisdiction."[97] Similarly, in *Illinois Bell II*, the Chief, Common Carrier Bureau, *inter alia*, dismissed the cross complaints filed by several Bell Operating Companies (BOCs) against AT&T that asked the Commission to require AT&T, the BOCs' customer with respect to certain shared network facilities, to pay the difference between any unlawful rates and lawful rates as subsequently determined by the Commission. The Bureau ruled that the Communications Act does not provide carriers with a private cause of action against their customers. The Bureau's ruling was upheld by the Commission on reconsideration. In the instant case, we are dealing with an issue fundamentally different from that presented in either *Thornell Barnes* or *Illinois Bell II*. The issue presented by MCI and contested by defendants is the extent to which MCI incurred any actual damages as a consequence of defendants' violations of a binding rate of return prescription. The focus of MCI's complaints is not defendants' individual interstate access rates *per se*, but the excessive earnings produced by these rates and their effect on MCI. We believe that it is reasonable to

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[97] 1 FCC 2d at 1275, citing *Laning-Harris Coal & Grain Co. v. St. L. & S.F. R.R. Co.*, 15 ICC 37 (1908).

inquire into MCI's overall purchase of interstate access services from defendants during the period in question for purposes of measuring MCI's damages that are attributable to defendants' violations of the rate of return prescription.

35. MCI's contention that the "filed rate doctrine" prohibits the allowance of offsets is similarly unpersuasive. According to MCI, the filed rate doctrine provides that a common carrier may only charge the rate on file with the Commission that is in effect at a particular time and may not retroactively raise such rate.[98] Therefore, MCI contends, allowing offsets would amount to a retroactive rate increase. Our task in these proceedings, however, is to determine whether MCI suffered any measurable damages that can be attributed to defendants' excessive earnings levels. As a measure of damages, MCI asks only that we compute the difference between what it paid for defendants' interstate access services and what it would have paid if defendants' rates had produced earnings within the Commission's prescribed levels. MCI does not allege that defendants' rates should have been set at a specific amount, nor does it claim that such a showing is necessary for purposes of its damages claims. In this context, where the focus is on earnings levels, not individual rates, we believe it entirely reasonable to examine the sum of MCI's purchases of interstate access services for purposes of assessing its damages claims. The cases that MCI relies upon for its claim do not support a contrary view. None of the cases involved a request for damages based on violations of a rate of return prescription.

36. In addition we reject MCI's claim that the allowance of offsets would somehow repeal our rate of return

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[98] MCI RBr. at 37, citing *Armour Packing Co. v. United States*, 209 U.S. 56, 81 (1907); *Pennsylvania R. Co. v. International Coal Mining Co.*, 230 U.S. 184, 196-197 (1913); *Lowden v. Simonds-Shield-Lonsdale Grain Co.*, 306 U.S. 516, 520-521 (1939); and *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577-579 (1981).

prescription on a category basis. The issue of damages to a particular complainant is separate and apart from the validity and effect of our rate of return prescription. The determination we make here is the extent to which complainant suffered damage on account of defendants' violations of the rate of return prescription. The question of offsets is relevant to that determination and no other.

37. Pacific Bell does, however, raise factors which it believes warrant an offset against MCI's damages claims. Pacific Bell states that it underearned on its common line services during the period in question and that MCI's prorated share of those underearnings is $1,296,000. In addition, Pacific Bell states that it has previously refunded approximately $498,000 to MCI in 1988 for switched traffic sensitive services overearnings. Pacific Bell argues that taking into account its underearnings and the previously refunded amounts, a net overcharge to MCI of approximately $413,000, based on the measure of damages advocated by MCI, results.[99] Additionally, Pacific Bell argues that it should be allowed to offset any damages awarded here against any undercharges to Telecom*USA, Inc., a subsidiary of MCI that has filed a separate complaint against Pacific Bell.[100]

38. USWC, on the other hand, did not provide any specific calculations or claims for offsets in its brief or

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[99] We note that MCI contends that Pacific Bell should pay damages in the amount of $2,210,851. Pacific Bell contends that the amount in question is approximately $2,207,000 before offsets. There is a difference of $3,851 between these amounts. This difference is due to rounding. MCI used the rate of return rounded to two decimal places (14.51%) as reported in Pacific Bell's Form 492. According to MCI, Pacific Bell calculated the rate of return to the nth decimal resulting in a slightly lower rate of return percentage. MCI RBr. at n.106. We will accept MCI's calculation based on Pacific Bell's reported rate of return.

[100] *See* Telecom*USA, Inc. v. Pacific Bell Telephone Company, File No. E-90-346 (filed May 29, 1990).

reply brief. It has provided, however, as Exhibit C to its brief, a chart listing what it describes as under- and overcharges to MCI and SBS based on earned rates of return of 12.75%, 13.10% and 13.25% for each individual operating company during the relevant monitoring period.[101]

39. We have carefully reviewed the arguments and evidence presented by the parties and believe that some offsets of the claimed damages amounts is appropriate. In the *MCI Liability Order*, we specifically rejected claims by the defendants that the Commission is required to take a carrier's interstate access underearnings as well as overearnings into account in determining whether a violation of the Act has occurred because this would be at odds with established case law.[102] We cannot, however, accept MCI's suggestion that we lack discretion in Section 208 proceedings to consider a complainant's overall purchase of interstate access services from the defendant during a particular monitoring period in assessing the damage or injury to that complainant.[103] We continue to believe, as courts have made clear, that carriers assume the risk of both losses for

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[101] USWC states that "MCI and USWC are continuing to work toward development of more precise market share numbers. When appropriate, we will update the numbers on our exhibits." USWC Br. at 19, n.50. No such updates have been provided to the Commission.

[102] *MCI Liability Order*, 5 FCC Rcd at 223, paras. 59-60, citing *Nader v. FCC*, 520 F.2d 182, 201 (D.C. Cir. 1975). *See also New England Telephone and Telegraph Co. v. FCC*, 826 F.2d 1101 (D.C. Cir. 1987), *cert. denied*, 490 U.S. 1039 (1989); and *AT&T v. FCC*.

[103] *See* para. 33, *supra*. We noted in the *MCI Liability Order* that the Constitution does not prohibit the Commission from ordering damages when a carrier has overearned on service category, citing the prevention of cross-subsidization as a long-recognized objective of rate regulation. *MCI Liability Order*, 5 FCC Rcd at 223, para. 57. We did not, however, preclude defendant carriers from raising circumstances surrounding a customer/complainant's purchase of interstate access, including those in other access service categories, as a defense to damages claims.

services they underprice and the prospect of returning amounts realized through rates that are unjustly and unreasonably high.[104] We also maintain our view that a carrier may properly be required to make whole those who have been injured by unlawful rates and practices without regard to whether the carrier has achieved its authorized rate of return overall.[105] Nevertheless, we believe it appropriate for purposes of assessing MCI's damages claims to examine MCI's overall purchase of interstate access services from the respective defendants during the period in question. Significantly, MCI does not dispute that, in its purchase of defendants' interstate access services, it benefitted substantially from defendants' rates that produced underearnings in one or more access categories. Nor does it dispute that defendants, consistent with the Commission's rate of return prescription requirements, could have lawfully effected changes in those rates in order to bring their earnings in line with the authorized level, resulting in higher charges to MCI.[106] Thus, while we view it as a reasonable starting point to look at the difference between the amounts MCI paid for defendants' access services on a category basis and the amount it would have paid if defendants had earned at the prescribed level for the relevant category, we find it also reasonable to offset payments by MCI that contributed to defendants' excessive earnings to the extent that it can be shown that MCI benefitted from defendants' undercharges during the relevant period.

40. We do not agree with MCI's contention that this approach results in unlawful cross-subsidization. Our decision here simply recognizes that although MCI has a legitimate claim for damages as a result of defendants' exceeding the rate of return prescription, it enjoyed offset-

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[104] *Id.* at 223, para. 58.

[105] *Id.*

[106] *See id.* at 223, para. 59.

ting benefits in the form of lower rates as well. We view offsets in the complaint context as appropriate only in relation to a particular complainant's purchase of access services from a defendant carrier. A defendant carrier would not, for example, be able to rely on undercharges to a separate customer or underearnings in general to offset a damage claim based on the measures adopted here. In particular, a complainant that takes service in only one access category that overearned would not have received the benefit of a defendant carrier's underearnings in access categories from which service is not taken.

41. Based upon our decision regarding the computation of damages here, we award damages to MCI from Pacific Bell in the amount of $416,851.[107] In reaching this amount, we have accepted MCI's calculation of Pacific Bell's overearnings as $2,210,851 for the switched traffic sensitive category. We have allowed the offset of undercharges in the common line category in the amount of $1,296,000 and the refund of switched traffic sensitive charges for the 1985-1986 monitoring period of $498,000 that was effected by Pacific Bell in 1988. Pacific Bell has made a showing, and MCI has not convinced us otherwise, that MCI recouped a portion of the excessive switched traffic sensitive charges in the form of the rate reduction effected by Pacific Bell in 1988 pursuant to the later-invalidated automatic refund rule. We will not, however, allow an offset of alleged undercharges to Telecom*USA, Inc. We note that at the time the Telecom*USA, Inc. complaint was filed, Telecom*USA, Inc. was not yet a subsidiary of MCI. The transfer of control to MCI was

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[107] As explained in para. 40, this amount is calculated as follows:

$ 2,210,851 (overcharges)

- 1,296,000 (undercharges—common line category)

- 498,000 (refund—switched traffic sensitive category)

$ 416,851 Damages

not approved until August 1, 1990.[108] In contrast, MCI's complaint against Pacific Bell was filed on February 9, 1988, nearly two years after the transfer of control of SBS to MCI was approved.[109] Telecom*USA, Inc. has properly filed a separate complaint. Accordingly, offsets. if any, may properly be asserted against Telecom*USA, Inc., in that proceeding and only in that proceeding.

42. We award damages to MCI from Northwestern Bell Telephone Company in the amount of $555,057.[110] In reaching this amount, we have accepted MCI's calculation of NWB's overearnings as $733,811 for the switched traffic sensitive access service category and $192,246 for

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[108] *See* Telecom*USA, Inc., Memorandum Opinion and Order, 5 FCC Rcd 4857 (Com.Car.Bur. 1990).

[109] *See* Application for Consent to Transfer of Control from IBM to MCI, Order and Authorization, Mimeo 2629 (released Feb. 14, 1986).

[110] As explained in para. 41, this amount is calculated as follows:

$ 733,811 (overcharges - switched traffic sensitive category)
192,246 (overcharges - special access category)
- 227,000 (undercharges to MCI - common line category)
- 21,000 (undercharges to SBS - common line category)
- 64,000 (undercharges to MCI - special access category)
- 2,000 (undercharges to SBS - special access category)
- 49,000 (undercharges to MCI - switched traffic sensitive category)
- 8,000 (undercharges to SBS - switched traffic sensitive category)
$ 555,057 Damages

NWB overearned in the switched traffic sensitive category in Iowa (14.64%), Minnesota (14.33%), Nebraska (15.79%), and North Dakota (19.71%) and underearned in South Dakota (11.76%). NWB overearned in the special access category in Iowa (14.31%), Minnesota (13.85%), Nebraska (13.63%), and North Dakota (16.01%) and underearned in South Dakota (9.21%). NWB underearned in the common line category in Iowa (12.47%), Minnesota (12.40%), Nebraska (12.25%), North Dakota (12.48%), and South Dakota (12.60%).

the special access service category. We have reviewed Exhibit C to USWC's brief [111] which sets forth calculations of MCI's and SBS's share of over- and underearnings at three rate of return levels. Based upon our review of the calculations provided by USWC at a 12.75% rate of return, NWB has shown that it is entitled to offset its overearnings in the switched traffic sensitive and special access service categories with MCI's and SBS's share of underearnings in the common line access service category of $248,000, in the special access service category of $66,000, and in the switched access service category of $57,000 for a total offset of $371,000.

43. Consistent with our decision regarding the computation of damages, we will not award damages to MCI from either PNB or MTN. The application of offsets by PNB and MTN to the amounts claimed as damages by MCI reduces those amounts to zero.[112]

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[111] Exhibit C contains a summary and compilation of USWC's over- and underearnings by rate element multiplied by MCI's market share to arrive at the dollar amount by which MCI over- or underpaid for element specific access services. USWC provided calculations at three rate of return levels—12.75%, 13.10%, and 13.25%.

[112] Accepting MCI's calculations for overearnings and USWC's calculations for undercharges at a 12.75% rate of return, these amounts are calculated as follows:

PNB

$ 262,727 (overcharges)

- 346,000 (undercharges to MCI - common line category)

- 51,000 (undercharges to SBS - common line category)

- 175,000 (undercharges to MCI - special access category)

- 5,000 (undercharges to SBS - special access category)

$ 0 Damages

MTN

$ 1,134,175 (overcharges)

- 753,000 (undercharges to MCI - common line category)

2. Interest on Damages Awards

a. Contentions of the Parties

44. Defendants' final claim is that MCI is not entitled to prejudgment interest should the Commission award damages to MCI. Pacific Bell grounds its claim on its contention that the amount of damages has been sharply disputed in these proceedings.[113] Pacific Bell claims that interest would penalize it even though it has not been accused of deliberate wrongdoing and interest is not necessary to make MCI whole. In addition, Pacific Bell argues that, should interest be awarded, it should accrue from the date on which it filed its final Form 492 report as the Commission has held that this is the point at which MCI is chargeable with the discovery of the facts on which its claim is based.[114] USWC simply contends that while the Commission may award interest under Section 204 of the Act, there is no provision for the award of interest under Section 206 of the Act. Because we cannot lawfully grant MCI a refund, USWC argues, we may not award interest.[115]

45. MCI disputes defendants' claims that it is not entitled to prejudgment interest at the IRS rate in connection with any ultimate damages award. MCI contends that an award of prejudgment interest is appropriate in the instant case because it is explicitly provided for in the parallel refund remedy under Section 204(a)(1) of the Act,[116]

- 121,000 (undercharges to SBS - common line category)
- 1,637,000 (undercharges to MCI - special access category)
- 50,000 (undercharges to SBS - special access category)

$ 0 Damages

[113] *See, e.g.*, Pacific Bell Br. at 19.

[114] *Id.* at 20, citing to *MCI Liability Order*, 5 FCC Rcd at 225, para. 78.

[115] USWC Br. at 12-13.

[116] *See* 47 U.S.C. § 204(a)(1), MCI RBr. at 45.

and is typically awarded in overcharge cases under the Act in order to make the injured party whole. MCI contends it is entitled to interest at the IRS rate from May 15, 1986 through July 30, 1992, of $1,947,537 from Pacific Bell and $2,046,105 from USWC.[117]

b. Discussion

46. The defendants' claim that the Commission lacks authority to award interest in a Section 208 common carrier complaint proceeding has no merit. Although Section 208 of the Communications Act does not explicitly authorize an award of interest, our authority under Sections 4(i) and other sections of the Act to award interest in a common carrier complaint case is well established.[118] In deciding whether to award interest in a particular common carrier complaint case we are generally guided by federal court practice, where the award of prejudgment interest ". . . is a matter left to the sound discretion of the trial court."[119] The award of interest in a common carrier complaint case is thus guided by considerations of fairness. Applying this criterion we believe that interest is appropriate in these cases.

47. Pacific Bell's claim that interest would unfairly penalize it even though it has engaged in no deliberate wrongdoing is unpersuasive. As we emphasized in the *MCI Liability Order*, the defendants enjoyed considerable flexibility in formulating the rates that are at issue in these complaints.[120] They were afforded ample opportunity to make mid-course corrections to bring their earnings levels in

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[117] MCI RBr. at Appendix D.

[118] *See* MCI Telecommunications Corporation v. American Telephone and Telegraph Company, *et al.*, 94 FCC 2d 332, 343-46 (1983).

[119] *United States v. California Board of Equalization*, 650 F.2d 1127, 1132 (9th Cir. 1981), *aff'd*, 456 U.S. 901 (1982), *reh'g denied*, 456 U.S. 985 (1982).

[120] 5 FCC Rcd at 223. *See, infra*, para. 29.

line with the Commission's prescription thereby avoiding the risks of being ordered to pay damages or refunds or effecting rate increases to remedy earning shortfalls.[121] Under these circumstances, we believe that as a matter of fundamental fairness, interest awards are appropriate irrespective of the motive or intent behind defendants' actions in exceeding the prescribed earnings level. Nor do we find merit in Pacific Bell's claim that interest is inappropriate because the amount of damages has been uncertain and sharply disputed. Defendants' earning levels were readily ascertainable at the time the complaints were filed, as was the extent to which those earnings exceeded the Commission's prescribed level. We are satisfied that MCI's complaints, which cite to defendants' excessive earnings as the basis for its damages claims, provided reasonable certainty of the amount of the damages it seeks.

48. We are left then with the question whether an award of interest in these proceedings is necessary to make MCI whole. We conclude that it is. MCI argues convincingly that it has been effectively deprived of the use of the excessive amounts it paid defendants as a result of defendants' unlawful rates while defendants, on the other hand, have enjoyed the beneficial use for a substantial period of time of funds to which MCI rightfully has claim. We are persuaded that interest is required not only to effect a full and fair remedy for MCI, which paid rates higher than it would have paid had defendants' earned within the prescribed levels, but also to avoid any unjust enrichment of defendants stemming from their charging rates that we have determined to be unjust and unreasonable under Section 201(b) of the Act.[122] We find, therefore, that MCI's request for interest computed at the IRS rate

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[121] *Id.*

[122] *See* New England Telephone and Telegraph Co. v. FCC, 826 F.2d 1101, 1113 (D.C. Cir. 1987), *cert. denied*, 109 S. Ct. 1942 (1989) (carriers may reasonably be required "to pay full interest for earnings they had no right to retain in the first place.").

for tax refunds is reasonable and appropriate and direct that such interest be computed on the damages awarded MCI in these proceedings from January 1, 1987, the day after which the 1985-1986 monitoring period ended,[123] until the date of full payment to MCI.[124]

IV. CONCLUSION

49. We have carefully reviewed the extensive record before us and have found, to the extent indicated here, that complainant is entitled to an award of damages, plus accumulated interest on such damages amount, for Pacific Bell Telephone Company's and Northwestern Bell Telephone Company's violations of our rate of return prescription for the 1985-1986 monitoring period.

V. ORDERING CLAUSES

50. Accordingly, IT IS ORDERED, pursuant to Sections 4(i), 4(j), 201, 206, 207, 208, and 209 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 154(j), 201, 206, 207, 208, and 209, that Pacific Bell Telephone Company SHALL PAY to MCI

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[123] At that point, defendants were subject to the earnings limitations of a distinct monitoring period.

[124] The applicable IRS rates are set forth in Appendix A. We believe that the rationale adopted by the Commission for applying the IRS rate in pole attachment complaint proceedings under Section 224 of the Act, 47 U.S.C. § 224, is equally applicable here. In Teleprompter of Fairmont v. C&P of West Virginia, 79 FCC 2d 232 (1980), the Commission stated

> As a matter of fairness, we believe that the rate of interest applied in a pole attachment complaint proceeding should be readily available, easily applied, and periodically revised to reflect changes in borrowing costs. In light of these considerations, we find the interest rate for federal tax refunds and additional tax payments suitable for use in this type of proceeding. This rate appears in a variety of easily obtained official and commercial publications, and is revised on a regular basis. [Footnote omitted.]

79 FCC 2d at 238.

Telecommunications Corporation the sum of $416,851 (Four hundred sixteen thousand eight hundred fifty-one dollars) within 60 days after release of this Memorandum Opinion and Order; and that Northwestern Bell Telephone Company SHALL PAY to MCI Telecommunications Corporation the sum of $555,057 (Five hundred fifty-five thousand fifty-seven dollars) within 60 days after release of this Memorandum Opinion and Order.

51. IT IS FURTHER ORDERED that Pacific Bell Telephone Company and Northwestern Bell Telephone Company SHALL PAY to MCI Telecommunications Corporation interest on the damages awarded here at the IRS rates set forth in Appendix A from January 1, 1987 until the date full payment is made.

52. IT IS FURTHER ORDERED that the Motions for Leave to File Out of Time filed by MCI on July 6, 1992 and July 14, 1992 ARE GRANTED.

53. IT IS FURTHER ORDERED that the Supplement to Motion to Dismiss filed by USWC on February 14, 1992 IS ACCEPTED for filing.

54. IT IS FURTHER ORDERED that the Application for Review filed by USWC on June 9, 1992 IS DENIED.

55. IT IS FURTHER ORDERED that the Motion for Summary Judgment filed by Pacific Bell on January 17, 1992, the Joint Motion to Dismiss filed by USWC on March 31, 1988, the Joint Supplemental Motion to Dismiss Complaint for Damages filed by USWC on April 11, 1990, the Motion to Dismiss filed by Pacific Bell on April 5, 1988, and the Motion to Dismiss Supplemental Complaint, filed by Pacific Bell on April 25, 1990, ARE DENIED.

FEDERAL COMMUNICATIONS COMMISSION

DONNA R. SEARCY
Secretary

APPENDIX D

[Filed Oct. 4, 1995]

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 93-1166

MCI TELECOMMUNICATIONS CORPORATION,
Petitioner

v.

FEDERAL COMMUNICATIONS COMMISSION, *et al.*,
Respondents

And Consolidated Cases

BEFORE: Edwards, Chief Judge, Wald and Ginsburg, Circuit Judges

ORDER

Upon consideration of Cincinnati Bell Telephone Company's, Petitioners in Nos. 93-1527, 93-1539 and 93-1541, Petition for Rehearing filed September 14, 1995, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT:
MARK J. LANGER
Clerk

By: /s/ Linda Jones
LINDA JONES
Deputy Clerk

APPENDIX E

[Filed Oct. 4, 1995]

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 93-1166

MCI TELECOMMUNICATIONS CORPORATION,
Petitioner

v.

FEDERAL COMMUNICATIONS COMMISSION, *et al.*,
Respondents

And Consolidated Cases

BEFORE: Edwards, Chief Judge, Wald, Silberman, Buckley, Williams, Ginsburg, Sentelle, Randolph, Rogers, and Tatel, Circuit Judges

ORDER

Upon consideration of Cincinnati Bell Telephone Company's, Petitioner in Nos. 93-1527, 93-1539 and 93-1541, Suggestion for Rehearing *In Banc*, and the absence of a request by any member of the court for a vote, it is

ORDERED that the suggestion be denied.

Per Curiam

FOR THE COURT:
MARK J. LANGER
Clerk

By: /s/ Linda Jones
LINDA JONES
Deputy Clerk

Circuit Judge Henderson did not participate in this matter.

APPENDIX F

[Filed Oct. 4, 1995]

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 93-1166

MCI TELECOMMUNICATIONS CORPORATION,
Petitioner

v.

FEDERAL COMMUNICATIONS COMMISSION, *et al.*,
Respondents

And Consolidated Cases

BEFORE: Edwards, Chief Judge, Wald and Ginsburg, Circuit Judges

ORDER

Upon consideration of Local Exchange Carriers' Petition for Rehearing filed September 14, 1995, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT:
MARK J. LANGER
Clerk

By: /s/ Linda Jones
LINDA JONES
Deputy Clerk

APPENDIX G

[Filed Oct. 4, 1995]

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 93-1166

MCI TELECOMMUNICATIONS CORPORATION,
Petitioner

v.

FEDERAL COMMUNICATIONS COMMISSION, *et al.*,
Respondents

And Consolidated Cases

BEFORE: Edwards, Chief Judge, Wald, Silberman, Buckley, Williams, Ginsburg, Sentelle, Ranholph, Rogers, and Tatel, Circuit Judges

ORDER

Upon consideration of Local Exchange Carriers' Suggestion for Rehearing *In Banc*, and the absence of a request by any member of the court for a vote, it is

ORDERED that the suggestion be denied.

Per Curiam

FOR THE COURT:
MARK J. LANGER
Clerk

By: /s/ Linda Jones
LINDA JONES
Deputy Clerk

Circuit Judge Henderson did not participate in this matter.